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Report

Development finance institutions: the need for bold action to invest better

Samantha Attridge and Matthew Gouett

April 2021

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Workers standing beside a drilling machine in Ghana. Photo: Daniel Mensah Boafo/Unsplash

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Acronyms

AAAA	Addis Ababa Action Agenda Financing for Development
AFD	Agence Française de Développement (French Development Agency)
AsDB	Asian Development Bank
CDC	CDC Group (formerly Commonwealth Development Corporation)
CGD	Center for Global Development
CIV	collective investment vehicle
DEG	Deutsche Investitions- und Entwicklungsgesellschaft (German DFI)
DFI	development finance institution
EDFI	Association of European Development Finance Institutions
EFTA	European Free Trade Association
EIB	European Investment Bank
ESG	environmental, social and governance
EU	European Union
FDI	foreign direct investment
FMO	Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (Dutch DFI)
GDP	gross domestic product
GNI	gross national income
HIC	high income country
IBRD	International Bank for Reconstruction and Development
ICT	information and communications technology
IDA	International Development Association
IFC	International Finance Corporation
IFI	international finance institution
IRR	internal rate of return
LDC	least developed country
LIC	low-income country
LMIC	lower middle-income country
MDB	multilateral development bank
MENA	Middle East and North Africa
MIGA	Multilateral Investment Guarantee Agency

NDB	national development bank
ODA	official development assistance
OECD	Organisation for Economic Co-operation and Development
OECD DAC	OECD's Development Assistance Committee
OPIC	Overseas Private Investment Corporation
RDB	regional development bank
ROA	returns on assets
SDG	Sustainable Development Goal
SME	small and medium enterprises
SSA	sub-Saharan Africa
UK	United Kingdom
UMIC	upper middle-income country
UN	United Nations
UNCTAD	United Nations Conference on Trade and Development
US DFC	United States Development Finance Corporation

Executive summary

The United Nations Addis Ababa Action Agenda (AAAA) on financing development is at a critical juncture. It was off track before the Covid-19 pandemic struck and there is now a very real risk that it will veer even further off course without bold corrective action. Covid-19 has served to dramatically increase development needs with 2020 marking the first increase in global extreme poverty (World Bank, 2020b), reversing two decades of progress. At the same time, development finance is under extreme pressure and at risk of decline. The Organisation for Economic Co-operation and Development (OECD) estimates that the Sustainable Development Goal (SDG) financing gap may balloon from $2.5 trillion[1] to $4.2 trillion, with a $700 billion year-on-year reduction of private capital inflows to countries eligible for official development assistance (ODA) (OECD, 2020d).

As policy-makers turn their attention to 'building back better' and mobilising the public and private resources required, there needs to be a clear understanding of why there has been so little progress in the past five years towards the ambition set in the AAAA. There must be clear assessments of what has worked and what has not – assessments based on a body of knowledge of the efficacy and impact of interventions prior to the Covid-19 crisis. The crisis has forced new thinking, but that thinking should critically engage with knowledge of the past.

To help inform this new thinking, this report focuses on one aspect — the mobilisation of private investment by development finance institutions (DFIs)[2] and the private sector operations of multilateral development banks (MDBs).[3] Private investment and a robust private sector are fundamental drivers of economic growth and job creation, which are key ingredients to help tackle poverty. DFIs and MDBs, with their core mandates to promote economic growth through investment, have been assigned a key role in supporting this agenda.

The report seeks to inform and anchor the discussion by providing the most up-to-date analysis of DFI and MDB investment and the private finance this investment has mobilised[4] in developing countries since 2013. It examines in detail the investment portfolios of 12 DFIs and MDBs who together mobilised more than 70% of the private finance reported to the OECD for the period 2017–2018.[5] It reflects on four crucial issues facing DFIs and MDBs as their role in the 'building back better' agenda is considered: the Covid-19 crisis response; the relationship between ODA and DFI/MDB investment; DFI and MDB investment in low-income countries (LICs); and the need for greater transparency from DFIs and MDBs.

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1 Note, all figures in this report are in US dollars unless specified otherwise.
2 For a definition of DFIs, see Appendix 1.
3 This report uses the term MDB to mean the private sector operations or windows of MDBs.
4 The terms 'mobilised', 'mobiliser' and 'mobilisation' are used throughout this report. The use of these terms is contentious because it implies that a DFI or MDB investment is additional because it caused private investors to invest when they would not otherwise have done so (Kenny, 2020a). Given the dearth of deal-level information provided by these institutions, claims of additionality are not substantiated by publicly released information. While the report uses the term 'mobilisation' because of its relevance in the parlance, it also recognises that it may misrepresent the actual import of DFI and MDB investment.
5 We deem this an appropriate level of coverage from which to draw insight on DFI and MDB investment patterns.

Key findings

Finding 1

DFI and MDB investment has grown each year but the pace of growth has been slow. Prospects for a material scale-up of new DFI and MDB investment do not augur well due to the economic fallout from Covid-19 and drastic declines in global foreign direct investment (FDI).

The amount of DFI and MDB commitments to mobilise private finance from our 12 selected institutions stood at just over $31 billion in 2018, an increase of 8.1% from 2013 to 2018, equating to an annualised rate of 1.6% ($467 million per annum). This growth, however, masks a surprising decrease in investment by some MDBs. Although total investment continues to grow, its pace is far off the mark from what is required to help significantly mobilise and scale private investment. Covid-19 has significantly increased the SDG public and private financing requirement but at the same time it is also likely that it has strained some DFI and MDB balance sheets. This, combined with the fact that DFIs and MDBs will be swimming against the tide of significantly reduced private investment in many developing countries, means that it will be a big challenge to significantly ramp up new DFI and MDB investment in 2021 and the near future. The reduction of foreign direct investment (FDI) was 45% globally and 16% specifically to developing countries in the first half of 2020 (UNCTAD, 2020b).

Finding 2

DFI and MDB mobilisation[6] has been increasing year on year and at a faster rate than growth in DFI and MDB commitments, resulting in increasing leverage ratios. This trend is being driven by MDBs. However, DFI and MDB investment is not yet mobilising private investment at scale. Lower levels of mobilisation are expected in 2021 due to the challenging external investment environment.

From a small base in 2012, private finance mobilised in developing countries by our 12 selected institutions increased by 42% from $14 billion in 2012 to $20 billion in 2018, equating to an annualised growth rate of 13%. Of particular importance is the welcome increase in mobilisation in LICs. Although starting from this small base, amounts mobilised have increased the fastest in LICs compared with lower middle- income countries (LMICs) and upper middle- income countries (UMICs). However, in 2019, mobilisation in developing countries declined and lower levels of mobilisation are expected in 2021 (IFC, 2021).

DFI and MDB mobilisation has been increasing at a faster rate than their investment, resulting in an increase in overall leverage ratios from 49 cents on the dollar to 69 cents on the dollar during the period 2013–2018. Leverage ratios for bilateral DFIs (82 cents) are higher than MDBs (52 cents) but MDB ratios appear to be increasing more quickly. This increase in MDB ratios is driven by a 53% increase in their direct mobilisation of private finance, from 2016 to 2018, accompanied by a surprising 7.4 % decrease in their total

6 Broadly, mobilisation refers to 'the ways in which specific mechanisms stimulate the allocation of additional financial resources to particular objectives. It implies a causal link between private finance made available for a specific project and the official flows that were used to incentivise them' (OECD, 2017). It should be noted that measuring mobilisation is a challenging issue due to differences in definition, scope and measurement methodologies (OECD, 2017).

commitments. This growth in MDB mobilisation and leverage appears to be driven by increasing use of new products that tap new types of investor, such as the use of unfunded risk transfer instruments and pooled mobilisation platforms (like the International Finance Corporation (IFC)-managed co-lending platform programme). Further study and data are required to fully understand this trend.

Despite these positive trends and the growth of environmental, social and governance (ESG) and impact investment more broadly, DFIs and MDBs are not yet mobilising large pools of institutional capital envisaged by them at the World Bank Annual meetings in 2016.

Finding 3

DFI and MDB investment is moving slightly down the country income spectrum, suggesting a small but welcome shift in the risk appetite of these institutions to invest in riskier countries. However, investment remains stubbornly low in LICs and is even lower in the poorest LICs.[7] This is a concern given the precipitous fall in FDI and the slow growth of gross domestic product (GDP) in LICs compared with LMICS and UMICs.

DFIs and MDBs have reallocated a percentage of their portfolio commitments from UMICs to LMICs. This is a welcome shift, but is mostly on a relative basis as UMICs received approximately the same level of DFI and MDB investment in 2018 as they had in 2013. For DFIs and MDBs, this has meant a higher relative exposure to countries with lower credit ratings, which may imply a small shift in their risk appetite. However, this implication cannot be confirmed as DFIs and MDBs do not disclose risk ratings for individual investments.

Alongside the modest growth of DFI and MDB total investment, investment in LICs has remained stubbornly low. In 2013, LICs welcomed 5.7% of DFI and MDB commitments; in 2018, it was 6.4% of commitments, an increase of $340 million in annual investments. However, over the same period, annual FDI inflows to these countries decreased by $11 billion, highlighting the limited countercyclicality of DFI and MDB investment in LICs. This, combined with slow annualised GDP growth of 2.9% (2013–2018), highlights the fact that the development of these countries has fallen behind, and Covid-19 exacerbates the risk that these countries will fall further behind.

Finding 4

Loans continue to dominate as the financial instrument of choice by MDBs and DFIs, and their importance in the product mix has increased since 2013. The use of guarantees remains limited but has increased slightly. The use of direct and indirect equity also remains limited but its importance has declined since 2013. This is of concern given the relatively small number of DFIs and MDBs that deploy equity and the financial and development additionality of this type of investment.

Except for MIGA, IDA, CDC and Norfund, debt finance continues to dominate the product mix of DFI and MDB portfolios, and this importance increased during the period 2013–2018. Given that much blended concessional capital is

7 Defined as the lowest decile based on a country's gross national income per capita. Deeper analysis found that countries in the lowest decile of per capita income received less than 2 cents of every dollar invested by DFIs and MDBs.

heavily deployed in the form of senior loans, it is reasonable to suppose that much of this own-account debt investment takes the form of senior debt, which is unlikely to meet the risk-mitigation needs of private investors, especially in LICs.

Only a relatively small number of DFI and MDBs deploy equity capital. In terms of portfolio share in 2018, the leading DFIs are Norfund (67.2%), CDC (55.4%), DEG (28.4%) and IFC (22%), although the equity share has decreased for CDC, Norfund and IFC – most noticeably for CDC, which has materially switched the instrument composition to include more debt, and for FMO, the equity share of which declined from 37.6% in 2013 to 8.9% in 2018. This trend is of concern given the relative scarcity and development additionality of equity investment, considering that equity markets are less developed than debt markets in many developing countries.

Guarantees mobilised the most private finance reported to the OECD. Although the use of guarantees has increased slightly since 2013 their use remains limited. Several factors are often cited for their limited use and include their accounting in the capital structure of DFIs and MDBs, their complexity and their high transaction costs, to name but a few. There is much interest in ramping up the use of guarantees to mobilise private investment; however, further evidence is required to understand their efficacy.

Finding 5

Effective policy-making is undermined by a lack of transparency and divergent measurement frameworks.

Although there has been some improvement in transparency and data disclosure by DFIs and MDBs, it remains a big problem and, in some areas, there has been a retrenchment. Semi- or disaggregated data on MDB and DFI mobilisation is not freely available and the quality and availability of data on investment commitment varies by MDB and DFI. The mobilisation and measurement frameworks of the MDBs/DFIs and the OECD differ and there is concern over double counting. This lack of transparency hinders accountability and thwarts informed analysis and ultimately effective policy-making. This situation is especially troubling as much DFI and MDB investment to mobilise private finance can be counted as ODA. Hard-won gains were secured with the aid effectiveness agenda and it is important that any ODA channelled in this way is subject to the same transparency requirements to enable effective scrutiny of its use.

Policy reflections and recommendations

DFIs and MDBs have been assigned an important role to mobilise private investment. It is clear from these findings that whilst progress is being made, it is falling far short of what is needed and well below the ambition embedded in the AAAA.

The findings of this report highlight that DFIs and MDBs are faced with an investment trilemma in meeting three expectations:

- to mobilise private investment at scale
- to create and pioneer markets, especially in the poorest countries, which involves taking on significant risks
- to remain financially viable – a task that has, without doubt, become more difficult in the current context.

The difficulties in navigating these competing challenges have been exacerbated by the economic shock resulting from Covid-19. Prior to the Covid-19 crisis, many DFIs and MDBs had little room for manoeuvre in terms of higher risk-taking

and materially scaling their investment, and this room is likely to tighten as the crisis strains MDB and DFI balance sheets.

Much DFI and MDB investment can be characterised as ad hoc and opportunistic, responding to individual investment opportunities. This is consistent with the profitability mandate of DFIs. However, there are limits to what this approach can achieve in terms of transformative impact or mobilising private investment at scale. This is likely to require greater risk-taking.

DFIs and MDBs are tasked with supporting market creation, but this requires a whole array of complementary actions. There are limits to what can be achieved through stand-alone investments. Complementary spending (through government or ODA financing) may be required in infrastructure or skills development. Policy or regulatory reforms may also be required to address investor concerns.

A strong understanding and robust public debate on how to manage these trade-offs implicit in the investment trilemma is currently undermined by a lack of transparency and inconsistent mobilisation measurement frameworks. Although progress towards data transparency is in the offing, progress on data alignment and methodological harmonisation has been slower. These efforts must be accelerated to meet the importance of this moment and provide policy-makers with the best information from which to take decisions.

What is clear is that DFIs and MDBs are at an inflection point. They have been tasked to achieve ambitious goals but their business models have been slow to adapt. At this critical juncture there is too much at stake to continue as usual. As policy-makers turn their attention from crisis response to next steps, shareholders urgently need to revisit the institutional objectives and business models of DFIs and MDBs, if these institutions are to help realise the ambition of the AAAA and the 'build back better' agenda. Tough decisions will need to be made on how best to allocate scarce development finance and these choices must be informed by a clear understanding of the effectiveness of MDB and DFI investment. Shareholders must recognise the trade-off between these three objectives and set clear and prioritised plans.

As recommended below, the relative emphasis placed on these objectives might be different across different country contexts. In LICs, greater emphasis could be placed on market creation, while in UMICs there is scope to improve mobilisation objectives.

Recommendation 1

DFIs and MDBs, their shareholders and donors should all rethink their impact objectives and investment approaches to focus more on transformative investment and market creation. This is especially important in LICs and LMICs.

DFI and MDB investment should act as market makers, focusing more on creating investment opportunities and markets than acting as market takers who respond to near-ready individual investment opportunities as they present themselves. This will require a shift from ad hoc and uncoordinated investment to strategic and coordinated investment, with market creation at its core. Fundamentally, investment will need to address two key constraints: weak enabling environments and lack of investible opportunities. This will have implications for the objectives

and business models of DFIs and MDBs, which shareholders should revisit. The achievement of this requires the following actions:

- Governments, donors and public sector operations of MDBs and regional development banks must step up efforts to support upstream policy reform and coordinate this with MDB and DFI investment.
- DFIs and MDBs should consider developing country investment strategies that demonstrate how they will set out to achieve market creation in countries and that clearly articulate how they will collaborate and coordinate with others.
- DFIs and MDBs should intentionally seek to develop and create investment opportunities, rather than invest in near-ready market opportunities. This requires an increased focus on pipeline development, pioneering, demonstration investments and early-stage investments, which in turn requires increased use of high-risk capital – for example, in the form of grants, equity, mezzanine financing including convertible finance and contingent grants, and guarantees.
- DFIs and MDBs should actively seek out, partner and build the capacity of suitable partners who can help build the investment pipeline, bring deals to the market, as well as tap and develop local capital markets. National development banks (NDBs), as an example, could play an important role here as well-run NDBs have unrivalled knowledge of local markets and long-standing relationships with local private and public sectors.

Recommendation 2

Efforts should be strengthened to make SDG investment in developing countries more accessible to institutional investors and to develop products that can mobilise private investment at scale. This requires a shift away from an approach focused on individual investment to a pooled portfolio approach.

In some markets, especially in the most challenging geographies, it may not be possible to mobilise private investment at scale in the short to medium term; here attention should be placed on making transformative investment. In the more developed markets, DFIs and MDBs are well placed to unlock the increasing interest of institutional investors to make ESG and more impactful investment, but this requires a shift towards pooled portfolio approaches.

MDBs and DFIs should make more use of pooled investment approaches that aggregate projects to meet the large ticket size investment requirements of institutional investors. Pooling also enables the diversification of risk and can include the pooling of higher risk LIC investment with lower risk UMIC investment. Pooling enables MDBs and DFIs to structure large-item products into tranches with differing risk profiles to meet the risk appetite of a range of institutional investors. Blended finance can be used to finance the higher-risk tranches. MDBs and DFIs with large balance sheets in diverse geographies and sectors are well placed to do this. Smaller DFIs may need to work with other DFIs to create the scale and diversification of pooled assets required. In doing so, DFIs and MDBs should be mindful of fragmentation and so they should work together to create a few large funds.

1 Introduction and overview

1.1 Introduction

Six years on from the United Nations Conference on Trade and Development (UNCTAD)'s 2014 *World investment report* (UNCTAD, 2014), which highlighted the $2.5 trillion funding gap to meet the United Nations (UN) SDGs and the AAAA, which followed in 2015, it is clear that financing for the UN SDGs has not met aspirations. In fact, with nine years to go until 2030, it has been disappointing how little progress has been made towards mobilising the public and private financing required to meet the SDGs. While the UN (n.d.) has reported increased levels of domestic resource mobilisation, ODA to developing countries has been increasing only moderately, and the poorest countries in the world have experienced significant declines in the amount of FDI inflows. By early 2020, five years had passed with little transformation in development finance as envisaged by the wide-ranging 'billions to trillions' agenda (World Bank, 2015).

As if this situation was not concerning enough, the global Covid-19 crisis has derailed any development progress that had been made. Development needs have increased dramatically, with 2020 marking the first increase in global extreme poverty in almost 25 years (World Bank, 2020b). This reversing of progress is likely to be exacerbated by the fact that development finance is under extreme pressure and at risk of decline. The OECD (2020d) estimates that the pandemic will force a $700 billion year-on-year reduction of private capital inflows to countries eligible for ODA. Combined with a $1 billion increase in Covid-19 related financing needs, the OECD states that the $2.5 trillion gap could balloon to $4.2 trillion, a gap that could be filled by aligning 1.1% of the $379 trillion in global financial assets under management. However, the task of aligning these assets is more difficult in this time of uncertainty in global financial markets, and previous experience suggests that this magnitude may be out of reach without fundamental change to financial systems.

To 'build back better' and mobilise the public and private resources required, there needs to be a clear understanding of why there has been so little progress in the past five years. There must be clear assessments of what has worked and what has not, assessments based on a body of knowledge of the efficacy and impact of interventions prior to the Covid-19 crisis. The crisis has forced new thinking, but that thinking should critically engage with knowledge of the past.

This report focuses on one aspect of this: the mobilisation of private investment by DFIs and MDBs. The SDGs and the AAAA marked a significant change in development thinking, placing emphasis on the complementary roles of the public and private sectors in achieving sustainable and inclusive economic growth. The SDGs explicitly recognise the central role of the private sector and private investment in this pursuit, and DFIs and MDBs, with their core mandates to promote economic growth through investment, have been assigned a key role in supporting this agenda. Since 2015, DFIs and MDBs are expected to meet three objectives:

- to mobilise private investment at scale, especially from institutional investors
- to create and pioneer markets, especially in the poorest countries, which involves taking on significant risks
- to remain financially viable.

However, this is a difficult conundrum for DFIs and MDBs given the trade-offs between these three

objectives, which must be better understood by shareholders (Box 1). As policy-makers turn their attention to 'building back better', and with accompanying calls for capital injections into DFIs and MDBs to increase investment, an urgent examination of their business models and future role is required. DFIs and MDBs must be given more realistic expectations that acknowledge these trade-offs and incorporate understanding of the settings in which they may hold a comparative advantage over other types of development finance. Business models will also need to change. Better aligned expectations based on a deeper evidence base are crucial to inform policy-makers attempting to effectively and efficiently allocate scarce public development finance.

This report seeks to inform the discussion by providing an up-to-date analysis of DFI and MDB investment and the private finance this has mobilised in developing countries between 2013 and 2018. DFIs and MDBs are a diverse group of institutions and this diversity is reflected in the countries and sectors in which they invest and the financial instruments that they employ.

The report highlights two trends having opposing impacts on the UN SDG funding gap. First, it notes welcome shifts in DFI and MDB investment and the resulting positive trends of slightly higher leverage rates (e.g. rates of mobilisation of private finance per dollar of DFI and MDB investment), increased investment in LMICs, and increased investment in riskier countries, suggesting a welcome shift in risk appetite down the country income spectrum. Second, it finds that total annual DFI and MDB investment commitments are growing quite slowly, LICs are continuing to receive a small share of investment commitments, and many DFIs and MDBs remain tied to employing instruments with which they have experience and capacity. The analysis of the ultimate impact of these trends is undermined by a lack in transparency of some DFIs and MDBs included in this report, a troubling observation given changes in reporting rules to the OECD Development Assistance Committee (OECD DAC), which incentivise more investment of ODA through bilateral DFIs, and the hopes pinned on these institutions to adequately respond to the Covid-19 crisis.

1.2 Overview

- Chapter 2 provides a brief outline of the scope, methodology and data sources used for Chapters 4, 5 and 6. A more detailed description of the methodology can be found in Appendix 1.
- The analysis starts in Chapter 3 by taking stock of the trends in external financial flows to developing countries to set the stage for the later analysis on DFI and MDB investment and mobilisation.
- Chapter 4 is an in-depth look at 2013–2018 DFI and MDB investment commitments. Relying on public data and data provided by the DFIs and MDBs, the commitments of 12 institutions are disaggregated by region, country income group, risk rating of the beneficiary country and financial instrument.
- Along similar lines, Chapter 5 presents the same type of disaggregation but focuses on the amounts of private finance mobilised by the same 12 institutions. This work offers a glimpse of which regions and countries are more attractive to private finance, and the influence that DFIs and MDBs can have over these private sector decisions.
- Chapter 6 combines commitment and mobilisation data from Chapters 4 and 5 respectively to ascertain the efficacy of DFI and
- MDB investment to catalyse private finance. By presenting how leverage ratios from 2012 to 2018 have shifted over time, insights are garnered as to the beneficiary countries that are most successful at welcoming much-needed private finance along with DFI and MDB investment.
- Finally, Chapter 7 concludes and reflects on the future of DFI and MDB investing.

Box 1 The investment trilemma

Development finance institutions (DFIs) and multilateral development banks (MDBs) are constantly facing trade-offs regarding their financial viability, the development impact of their investments and their ability to mobilise private finance at scale in developing countries. However, it is the owners and shareholders of DFIs and MDBs that set the mandate and the orientation of how these institutions balance the trade-offs. Unfortunately, it is not clear whether the stakeholders and those that set mandates fully understand how these trade-offs can constrain outcomes. This can result in misunderstanding what DFIs and MDBs can and cannot do and in misaligned expectations.

One example is the trade-off between increased development impact and financial return, especially where higher risk can increase development impact. Investing in the riskier tranches of the capital stack of an investment and creating markets in low-income countries (LICs) and lower middle-income countries (LMICs) by investing in pioneering and early-stage investment is frequently cited as triggering some of the most important impact outcomes that DFIs and MDBs can have; it also has the highest risk for loss by the investor. Should DFIs be constrained by financial viability and/or profitability targets that either eliminate or constrain such high-risk investment? The data in this report indicate that there continues to be a reliance by DFIs and MDBs on making loans and investing in upper middle-income countries (UMICs), the safest parts of the DFI and MDB investment market. While a loan to a manufacturing firm in a UMIC will no doubt create formal jobs and elicit other follow-on impacts, the likelihood of that investment eventually attracting private capital is higher than a start-up in a LIC receiving a private investment. However, DFIs and MDBs view that 'safe' loan as crucial to meeting their financial targets – targets that are put upon them by their owners or the discipline of their funding models.

Other examples of trade-offs that need to be considered and understood are the pursuit of increased mobilisation, which may clash with the need to be additional, and the trade-off between mobilisation and DFI and MDB lending targets where there is a limited deal flow, especially in the poorest countries.

DFI owners and MDB shareholders must be clear with themselves about their priorities and how they want their agents, the DFIs and MDBs, to pursue them. DFIs and MDBs are not homogeneous in their funding, capacity, or relations with their owners and shareholders, so how they balance this trade-off will not be the same. Still, DFIs and MDBs and their stakeholders must be forthright with one another and clear in the objectives being pursued, as well as how those objectives are being incentivised among their staffs. If DFIs and MDBs are to be governed by pursuing outcomes, it must be clear what those outcomes are and how they are prioritised.

2 Scope and methodology

As noted in our previous work (Attridge and Engen, 2019), definitions and methodologies associated with DFI investment and mobilisation of private finance are numerous and varied; consequently, data analysis in this area is challenging. Further compounding this challenge is the issue of poor data availability and a lack of transparency. It is therefore important at the outset to briefly outline the scope, methodology and source data used in the analysis of Chapters 4, 5 and 6. A more in-depth discussion of the methodology of this analysis is available in Appendix 1.

2.1 Scope

This research seeks to analyse DFI and MDB investment to mobilise private investment supported by their own account resources and covers their total private investment portfolios. As such we refrain from the use of the term 'blended finance' in this report, as DFIs and MDBs understand this term in the narrow sense of blending external concessional resources with their normal own accounts (a minority of their operations). Most DFI and MDB investment to mobilise private investment is funded by their own account and this is the focus of our analysis.

Not all MDBs and DFIs are included in the analysis. Our sample 12 MDBs and DFIs cover more than 70% of the total private finance mobilised, as reported in the OECD mobilisation survey for the 2017–2018 period (OECD, 2020b). Whilst not comprehensive, it is deemed an appropriate level of coverage from which to draw insight on DFI and MDB investment patterns.

2.2 Data

2.2.1 Commitment data

The commitment analysis is based on investment information provided by 12 DFIs, seven of which are bilateral DFIs and five of which are multilateral institutions. Investment information from CDC Group and United States Development Finance Corporation (US DFC) was downloaded from their websites, while Deutsche Investitions- und Entwicklungsgesellschaft (DEG), Nederlandse Financierings-Maatschappij voor Ontwikkelingslanden N.V. (FMO), Norfund, Agence Française de Développement (AFD) and Proparco provided non-public investment information.[8]

The data gathered for the Asian Development Bank (AsDB), European Investment Bank (EIB),[9] International Development Association (IDA),[10] International Finance Corporation (IFC) and Multilateral Investment Guarantee Agency (MIGA) were sourced from their respective public disclosures.

8 Note that while AFD and Proparco provided information for investments made during the 2016–2018 period, their commitment data were imputed for 2013–2015 (see Appendix 1 for more details). Moreover, the calculated totals from the data provided for 2016–2018 did not reconcile to the amounts recorded in their annual reports. Calculated totals were, on average, 13% less than annual report totals for 2016–2018.

9 For investments made by EIB, only investments in non-European Union and non-European Free Trade Association countries were considered.

10 For IDA, only partial risk guarantees are included in the analysis.

It is important to note that among the investments made by the 12 institutions outlined above, not all investments were included in the analysis. This report focuses on financing commitments that mobilise private finance. To identify these commitments, investments were assessed individually to ascertain whether they were mobilising or not. Moreover, only non-sovereign operations were determined to be mobilising; sovereign operations were excluded as it was assumed that these did not involve private financiers. The criteria for inclusion and exclusion are discussed further in Appendix 1, but 72% of the total investment volumes for these institutions were classified as mobilising.[11]

2.2.2 Mobilisation data

There are two main sources of data on DFI and MDB mobilisation. The first source is data that DFIs and MDBs report to the OECD using OECD mobilisation methodologies. The second source is the data that MDBs and DFIs have been reporting annually since 2016 in a joint report using their own mobilisation methodologies. Due to data availability and levels of disaggregation, different sources of mobilisation data inform our analysis (Table 1). Data provided by the OECD could not be disaggregated on an annual basis for the 2012–2015 period. For the analyses in Chapter 5 and Chapter 6, the amounts mobilised during this period are presented as an annual average to allow for a limited trend analysis.

Also, the 2012–2015 data provided by the OECD listed the country that mobilised the private finance, not the individual agency within the country. However, the 2016–2018 data provided by the OECD did offer this nuance. To adjust for this difference, the share of a country's mobilised private finance in 2016–2018 accounted for by a DFI was also applied to the 2012–2015 data. For example, CDC Group accounted for 70.6% of private finance mobilised by the UK for 2016–2018, so the 2012–2015 amounts were adjusted so that CDC Group accounted for 70.6% of these amounts.

Furthermore, DEG, FMO and IDA are not included in the analysis of mobilisation efforts. For DEG, this is due to them only reporting the amount of climate-related private finance mobilised to the OECD, which would, comparatively, underreport its total mobilisation efforts. Similarly, FMO only reports amounts mobilised from their guarantees and from syndicated loans for which they are the lead arranger.[12] For IDA, its mobilisation efforts in 2012–2015 are reported as aggregated with the International Bank for Reconstruction and Development (IBRD). Without a way to disaggregate IDA mobilisation from IBRD mobilisation it is likely that the IDA mobilisation efforts would be overstated.

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11 Appendix 2 offers a breakdown, by DFI and MDB, of the volumes considered to be mobilising. This issue mainly affects three institutions (AFD, IFC and EIB). AFD provided data on its entire development finance portfolio and included traditional ODA projects, such as sovereign operations (which are not considered as mobilising commitments). The case of EIB was similar as its database also included sovereign operations. IFC's lower rate of mobilising commitments may be due to instances in which the IFC commitment was equal to the total project value and private investment was not disclosed (due to confidentiality or because the purpose of the disclosed investment was to build future investment pipeline for which IFC commitment was total project value).

12 Although, for 2018, OECD data included FMO mobilisation through all of its activities.

Table 1 Source data for development finance institutions and multilateral development banks

	Commitment data	Mobilisation data
Bilateral DFIs		
CDC Group	Public disclosure	OECD
DEG	Provided privately	OECD, but not used
FMO	Provided privately	OECD, but not used
OPIC/US DFC	Public disclosure	OECD
Norfund	Provided privately	OECD
AFD	Provided privately (imputed 2013–2015)	OECD
Proparco	Provided privately (imputed 2013–2015)	OECD
Multilateral institutions		
AsDB	Public disclosure	OECD (2012–2015), MDB report (2016–2018)
EIB	Public disclosure	OECD (2012–2015), MDB report (2016–2018)
IDA	Public disclosure	OECD (2012–2015), MDB report (2016–2018), but not used
IFC	Public disclosure	OECD (2012–2015), MDB report (2016–2018)
MIGA	Public disclosure	OECD (2012–2015), MDB report (2016–2018)

For the period from 2016 to 2018, the OECD could not provide semi-disaggregated data on the amounts mobilised by the multilateral institutions because of confidentiality agreements. In its place, the disaggregated private direct mobilisation figures disclosed in the annual MDB *Mobilization of private finance* report were included (IFC, 2019). We use direct mobilisation figures as this captures the mobilisation as a result of the 'active and direct involvement' of the MDB and so causality is clear (IFC, 2021). We exclude indirect mobilisation figures as causality is less clear. Although the methodology between the two reports differs (including definitions and classifications), the reluctance of the multilateral institutions to share semi-disaggregated data due to investment confidentiality offered little alternative if this type of analysis is to be conducted. Caution should therefore be taken in interpretation as there is disagreement between the OECD and the MDBs on methodological issues and concern about double counting with the MDB report methodology (Attridge and Engen, 2019). This underscores the need for a harmonised reporting system (Attridge and Engen, 2019). Table 2 summarises which DFIs have been included in each chapter.

Table 2 Development finance institution and multilateral development bank data included in this report

	Chapter 4: DFI and MDB investment in developing countries	Chapter 5: Mobilisation of private investment to developing countries	Chapter 6: DFI and MDB leverage ratios
Bilateral DFIs			
CDC Group	✓	✓	✓
DEG	✓	–	–
FMO	✓	–	–
OPIC/US DFC	✓	✓	✓
Norfund	✓	✓	✓
AFD	✓	✓	✓
Proparco	✓	✓	✓
Multilateral institutions			
AsDB	✓	✓	✓
EIB	✓	✓	✓
IDA	✓	–	–
IFC	✓	✓	✓
MIGA	✓	✓	✓

3 External financing flows to developing countries

Key findings

- FDI is the most significant inflow into UMICs; remittances are the most significant inflows into LMICs; and ODA is the most significant inflow to LICs.
- Annual FDI flows to LICs have been decreasing significantly.
- The region that has experienced most of the FDI decline is Latin America & Caribbean.
- Richer developing countries benefit more from FDI than ODA; ODA to LICs has seen a small increase but has not offset the significant decline of FDI flows to LICs.

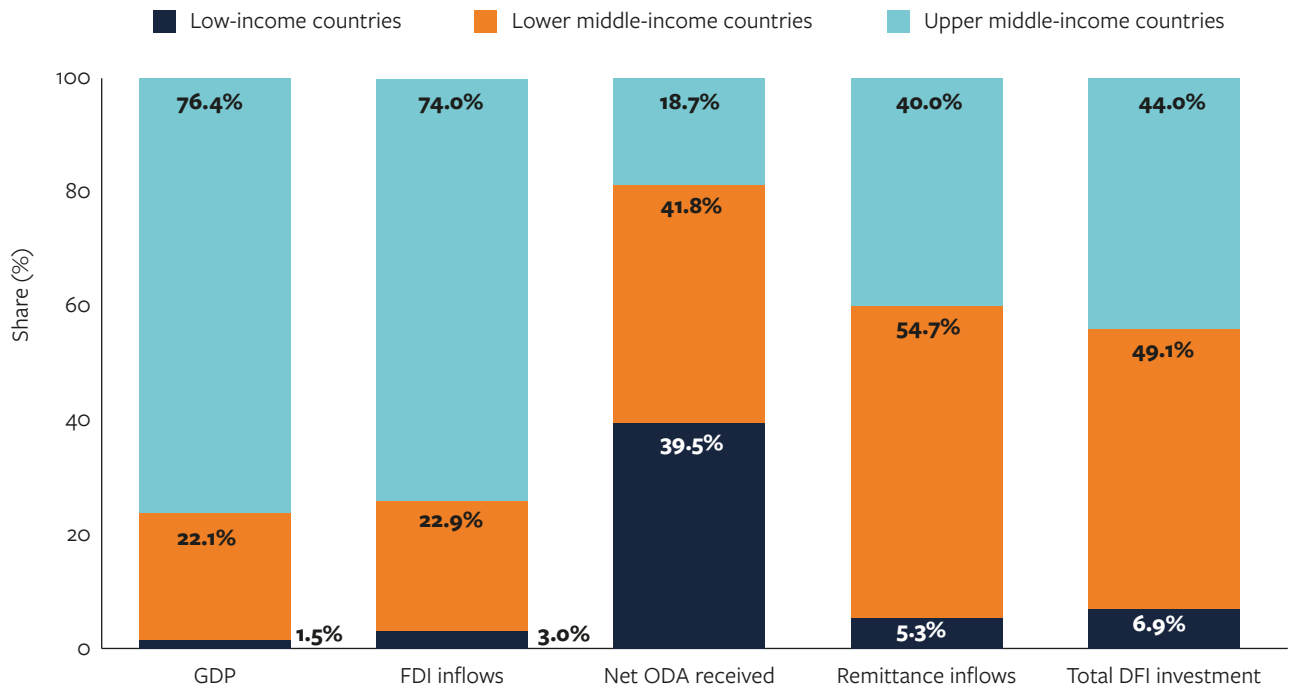
Even prior to the Covid-19 crisis, it was evident that the wide-ranging 'billions to trillions' agenda and the journey to filling the UN SDG funding gap was off to a disappointing start. Ever since UNCTAD's 2014 *World investment report* outlined the funding gap, there has been a greater acknowledgement of the role of the private sector and the urgent need to mobilise private investment in developing countries (UNCTAD, 2014) as a complement to public investment, both domestic and international. While private investment has a significant role in filling this gap, it is not the only source of external finance into a country and the composition of these flows varies by country income group.[13] This chapter provides a brief overview of the relative importance of different external financial flows by country income group. We also look at trends in external financial flows as a background context for DFI and MDB investment to mobilise private investment.

3.1 Composition and trends in external financing flows by country income grouping

FDI mostly flows to UMICs consistent with their share of developing country GDP. Similarly, LMICs welcome a consistent share of FDI inflows relative to their GDP, but also welcome a much larger share of net ODA and remittance inflows. LICs welcome double the share of FDI inflows as could have been expected based on their GDP (Figure 1). To illustrate further the importance of different flows to countries in different income groups, Figure 2 illustrates external financing flows on a per capita basis. As would be expected, LICs are most dependent on net ODA and attract less FDI inflows and remittance inflows. LMICs and UMICs have higher levels of FDI and remittance inflows even when adjusted for their population. With UNCTAD (2020b) estimating a 16% decrease in FDI flows to developing economies in the first half of 2020 due to the Covid-19 pandemic, it is likely that this decline will be uneven across country income groups and that the composition of external finance illustrated in Figures 1 and 2 is likely to change in the future.

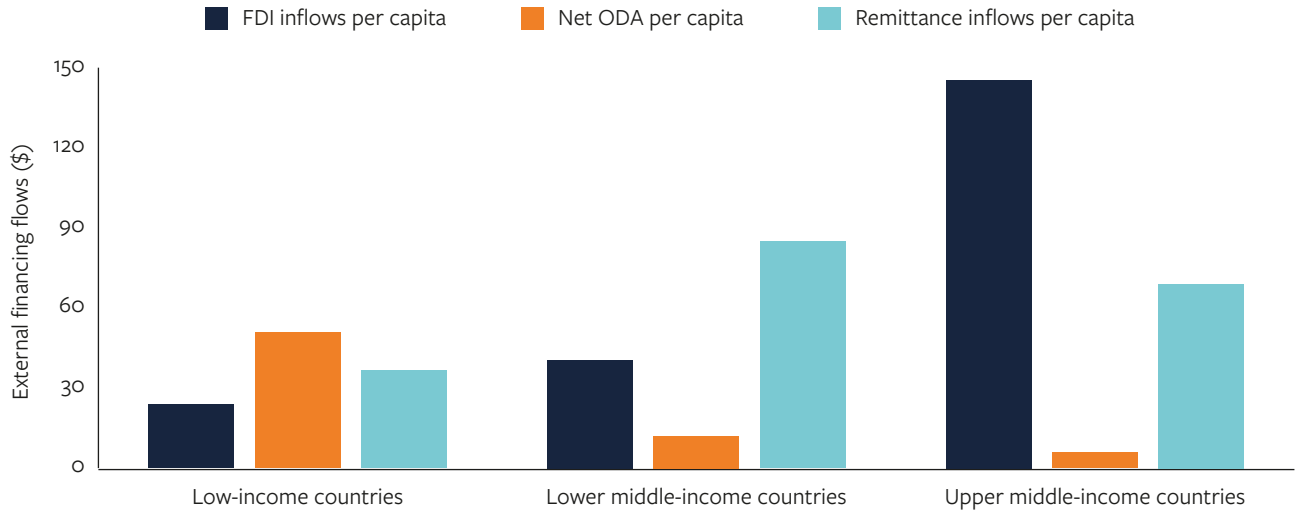
13 During the period under review, countries moved between income classifications. To control for this effect, in this chapter we use the income classification of the country in 2018 according to the World Bank country income classification and hold this constant through 2013–2018.

Figure 1 Shares of developing country GDP and external financing flows to developing countries, 2013–2018



Notes: Data only includes flows for which the beneficiary country is named. Total DFI investment from ODI dataset, based on authors' calculations, does not include AFD commitments.
Sources: FDI inflow data from UNCTAD (2020a), net ODA data from OECD (2020a), and GDP, population and remittance inflow data from the World Bank (2020)

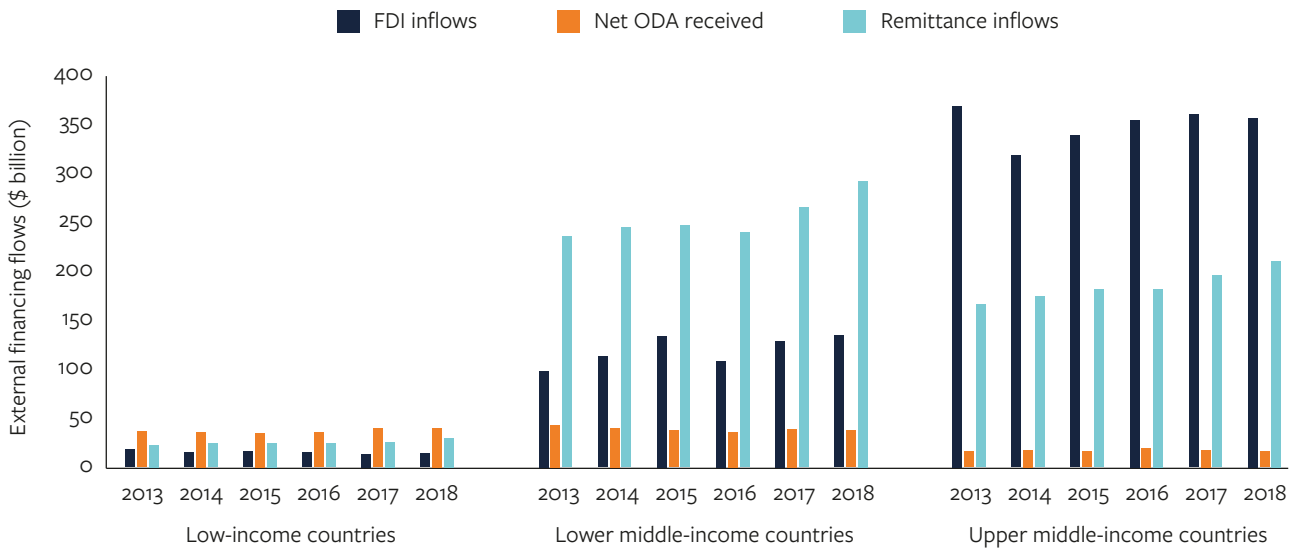
Figure 2 External financing flows to developing countries per capita, 2013–2018



Notes: Based on authors' calculations. Data only includes flows for which the beneficiary country is named.
Sources: FDI inflow data from UNCTAD (2020a), net ODA data from OECD (2020a), population and remittance inflow data from the World Bank (2020)

Despite these relative figures, on a total basis, the differences between income groups is even more striking (Figure 3). Whereas LICs benefit from similar levels of FDI inflows, net ODA and remittances, LMICs benefit far less from net ODA than from FDI inflows and remittance flows. Even more striking is how much UMICs receive in FDI relative to remittance flows and net ODA. Figures 1, 2 and 3 provide a clear illustration that the importance and influence of private investment flows vary among countries in the different income groups and point to challenges and opportunities that DFIs may face when trying to catalyse private investment in different country income groups. Trends in external flows are not encouraging (Table 3). Overall, FDI has barely grown, with overall annualised growth rates of just 0.8% from 2013 to 2018. Net ODA[14] to developing countries decreased by 0.3% annually (OECD, 2020a) from 2013 to 2018. As can be seen from Table 3, these trends have been felt differently by different country income groups and, considering annualised GDP growth rates, serve to reinforce widening disparities between country income groups and their reliance on different forms of external financial flows. For example, LICs, which were already more dependent on ODA, had their net ODA grow by 1.9% annually, but the amount of FDI they received decreased by 5.0% annually. Over the same period, FDI to UMICs decreased slightly (0.7% annually), but remittances grew at almost 5.0% per year. LMICs, for their part, welcomed much higher levels of FDI and remittances in 2018 than they had in 2013, more than offsetting the decline in net ODA.

Figure 3 External financing flows to developing countries, 2013–2018



Note: Based on authors' calculations.

Sources: FDI inflow data from UNCTAD (2020a), net ODA data from OECD (2020a), and remittance inflow data from the World Bank (2020)

14 Net ODA is gross ODA that a recipient receives in a given year less repayments of the principal on loans received in prior years, as well as offsetting entries for forgiven debt and grant recoveries. For the purposes of this chapter, net ODA figures are flows from OECD DAC member countries and multilateral donors.

Table 3 Annualised growth rates of GDP and external flows, by country income group and region, 2013–2018

	GDP (%)	FDI inflows (%)	Net ODA	Remittance flows (%)
Country income category				
LICs	2.9	–5.0	1.9	5.1
LMICs	4.0	6.5	–2.6	4.4
UMICs	4.2	–0.7	0.0	4.9
Region				
East Asia & Pacific	7.0	2.3	–8.8	4.2
South Asia	7.9	8.9	–0.3	3.5
Sub-Saharan Africa	–0.2	–2.0	0.1	5.0
Middle East & North Africa	–8.4	–1.6	5.2	3.5
Europe & Central Asia	10.9	2.2	–4.7	4.6
Latin America & Caribbean	–3.6	–2.7	1.7	7.8
All developing countries	**4.2**	**0.8**	**–0.3**	**4.6**

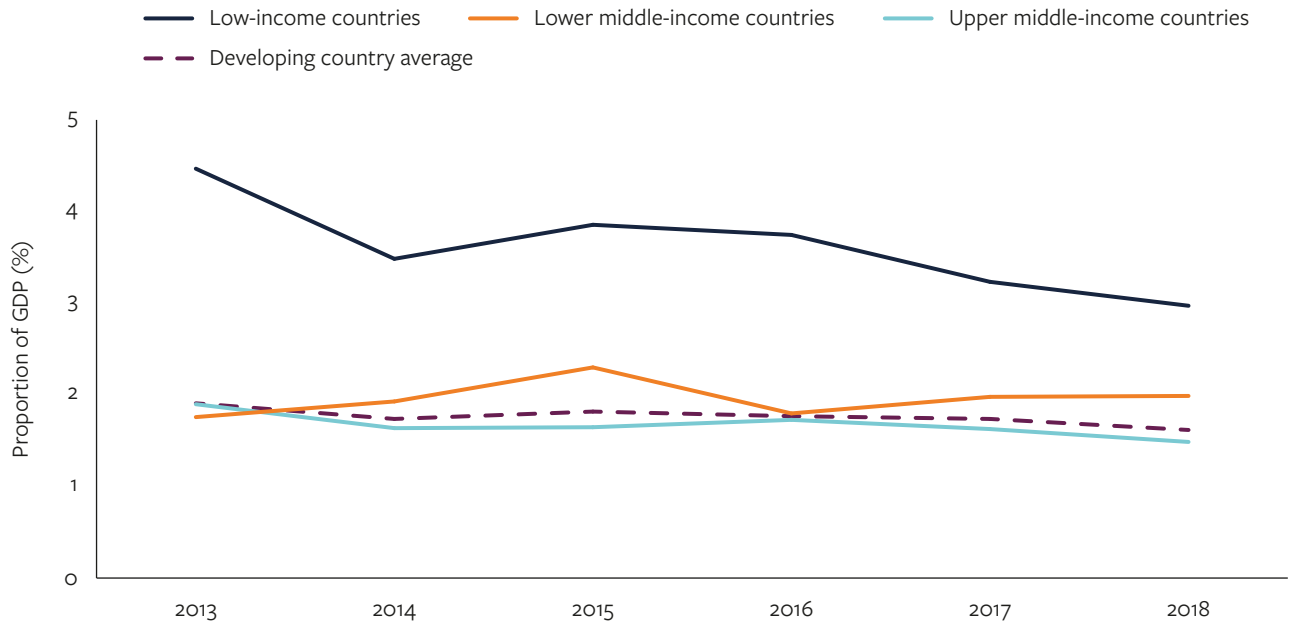
Sources: FDI inflow data from UNCTAD (2020a), net ODA data from OECD (2020a), and GDP and remittance inflow data from World Bank (2020a)

3.2 Trends in foreign direct investment

Focusing further on FDI to developing countries, from 2013 to 2018, the total GDP of developing countries grew by 4.2% annually; however, FDI flows to these countries only increased by 0.8%. This growth in FDI flows was driven by investment in LMICs, which grew at an annualised rate of 6.5%. Far more concerning is the annual decline of 5.0% that LICs experienced during the period. In 2018, FDI inflows to LICs were 23% less than in 2013, the exact opposite trend of what the AAAA seeks to encourage. Given the urgent need to inject private investment in LICs to help fuel growth, this decline is of concern. As LICs have smaller domestic economies and are more dependent on FDI inflows than LMICs and UMICs to add to country wealth (Figure 4), this decline is even more problematic.

Figure 4 illustrates that for UMICs, GDP increased proportionally faster than FDI inflows; hence FDI inflows as a proportion of GDP decreased. So, despite FDI inflows increasing in these countries, the relative increase in GDP was higher. For LICs, this was not the case; FDI inflows decreased significantly and GDP grew modestly. The FDI inflow decrease to LICs of 23% from 2013 to 2018 far outweighed the 16% increase in GDP over the same period. Therefore, while Figure 4 shows the decline of importance of FDI on the GDP of all developing countries, there is a significant difference in the impact of this in LICs when compared with other developing countries. Regionally, the decline of FDI inflows is less clear. Annual inflows to developing countries grew annually in South Asia (8.9%), East Asia (2.3%) and Europe & Central Asia (2.2%), whereas these flows declined in Middle East & North Africa (–1.6%), sub-Saharan Africa (–2.0%) and Latin America & Caribbean (–2.7%) (Table 3).

Figure 4 FDI inflows as a proportion of GDP, by country income group, 2013–2018



Note: Based on authors' calculations.

Sources: FDI inflow data from UNCTAD (2020a) and GDP data from the World Bank (2020)

This decrease in flows to sub-Saharan Africa (SSA) was felt by small and large countries alike. Of the 10 sub-Saharan countries that attracted the most cumulative FDI from 2013 to 2018, seven countries attracted less in 2018 than they did in 2013.

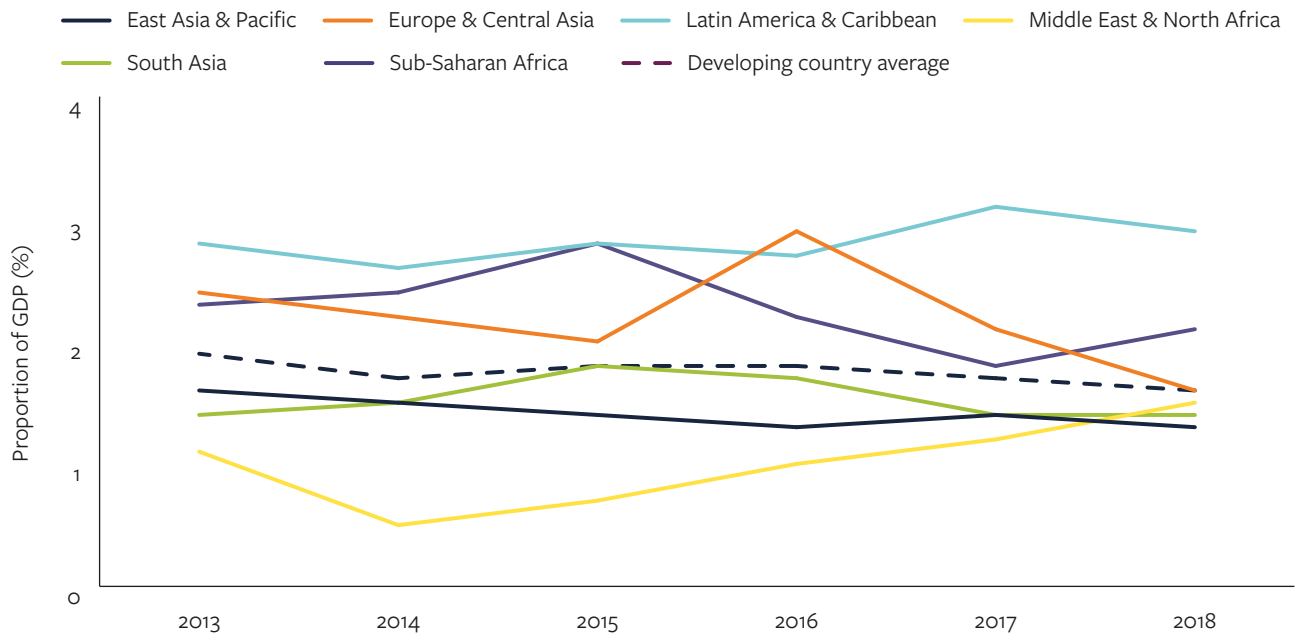
Although the decrease in FDI to SSA during this period is likely linked to the decrease in commodity prices and the reliance of these countries on the extractive industries, the fact remains that investment capital to these countries slowed dramatically.

As with before, Figure 5 shows that gross FDI inflow changes do not tell the entire story. When compared with changes in GDP, the increase in FDI inflows to Europe & Central Asia was outpaced by the increase in GDP; thus, the developing countries in the Europe & Central Asia region experienced the most significant relative decline in FDI inflow to GDP. The story was a similar one for the countries of East Asia & Pacific. By contrast, GDP growth in SSA stagnated (an annualised increase of less than 0.2%) and FDI declined; thus the importance of FDI inflows to SSA GDP has dwindled. The increases in the importance of FDI inflows to the GDP of developing countries in Latin America as well as the Middle East and North Africa regions were due to FDI inflows declining less than GDP over the 2013 to 2018 period.

As highlighted earlier, the tenuous situation facing developing countries starved of private investment has worsened due to the Covid-19 crisis. As mentioned above, in October 2020, UNCTAD (2020b) reported that FDI inflows to developing countries had decreased by 16% in the first six months of 2020; however, in line with previous years, FDI to countries in Africa decreased by 28%. While there will, no doubt, be a critical role for DFIs in these markets during the recovery, it must be acknowledged that the

job of DFIs in these countries has become more difficult considering these trends. Recovering to pre-crises levels of FDI inflows will not be enough for the countries that have faced years of decline, and DFIs and their shareholders need to review approaches in these markets.

Figure 5 FDI inflows as a proportion of GDP, by region, 2013–2018



Note: Based on authors' calculations.

Sources: FDI inflow data from UNCTAD (2020a) and GDP data from the World Bank (2020)

4 Trends in development finance institution and multilateral development bank investment in developing countries

Key findings

- DFI and MDB investment growth has been slow, growing at an annualised rate of just 1.6% during 2013–2018. It has grown at a similar rate to that of net ODA and faster than FDI flows to developing countries.
- Regionally, DFIs and MDBs have reallocated investment away from Europe & Central Asia to the Middle East & North Africa, South Asia and investments classified as regional.[15]
- DFI and MDB investment in LICs has remained stubbornly low despite an increased need for capital as FDI inflows to these countries declined significantly.
- Investment in UMICs is concentrated in countries on the cusp of being classified as high income.
- DFIs and MDBs are increasingly investing in countries that are higher risk, suggesting an overall increase in risk appetite.
- Over 70% of DFI and MDB investment goes to countries that have sovereign risk ratings within six ratings of being classified as investible.
- With the exception of MIGA and IDA, debt finance continues to dominate the product mix of DFI and MDB portfolios, and this importance increased during the period 2013–2018.

DFIs and MDBs must juggle and balance three intertwined issues: financial viability, development impact and mobilisation. Portfolio allocation is an outcome of this balancing act but is also conditioned by operational competencies and the mandates given to these institutions by their owners. Although it seems as if bilateral DFIs operate more independently than many government agencies, they do remain accountable to the mandate set by their shareholder governments, mandates that change due to economic imperatives, political shifts and global crises. This chapter explores recent DFI and MDB portfolio allocation patterns to understand how DFIs, MDBs, and their owners, have responded since the launch of the AAAA and the accompanying increased emphasis on DFI and MDB investment to mobilise private investment. The reader is reminded that this analysis is based on our selected sample of 12 DFIs and MDBs that mobilised 70% of the total private finance mobilised in 2017–2018 that was reported to the OECD.

4.1 Total DFI and MDB investment trends

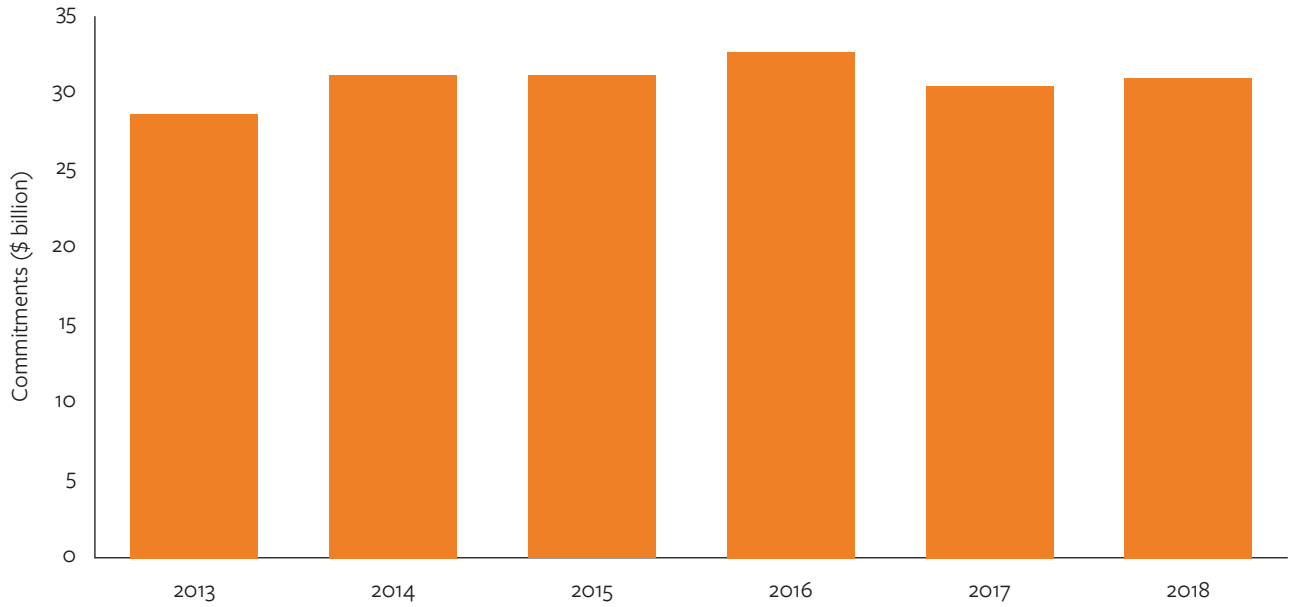
Despite the rhetoric, new DFI capitalisations and blended finance initiatives, total mobilising commitments by our sample DFIs and MDBs have grown at a very slow pace. Commitments from the sample institutions have only grown from $28.7 billion in 2013 to $31 billion in 2018 (Figure 6). This annual growth of 1.6% is the same as the 1.6% growth of net ODA to developing

15 Investments for which a specific beneficiary country is not named.

countries and is slightly more than the 0.5% growth in FDI to developing countries.[16] So, while there is an acknowledged and urgent need for more DFI and MDB investment, the anticipated material change in the level of investment required has not yet materialised.

A combination of factors may account for this on the supply and demand side.[17] Focusing on the supply side, DFIs are heterogeneous in their operations, funding models and governance structures. As a result, the extent to which DFIs and MDBs invest increases in their available capital varies and is determined by a number of factors including funding models and associated capital adequacy requirements and/or shareholder directives. A quick look at the balance sheets of IFC and CDC Group illustrates these issues. In 2018, 44.7% of IFC's assets were its investments to mobilise private investment. The remaining assets were invested in liquid assets for risk management and capital adequacy purposes. This is in contrast to CDC's investments to mobilise private investment, which accounted for 74% of its assets in 2018. Given that IFC issues debt on the international capital markets and is expected to maintain its 'AAA' bond rating, it carries more non-investment assets on its balance sheet than CDC, which is wholly funded by the UK government.

Figure 6 Annual mobilising commitments, 2013–2018



Source: Authors' calculations based on the ODI dataset

16 Note that the annualised growth of net ODA of 1.6% includes net ODA for which the developing country is unspecified and, for this reason, differs from figures reported in Table 3.

17 In this discussion, 'supply' refers to finance looking for investment opportunities (i.e. DFI, MDB and private capital) and 'demand' refers to investment opportunities requiring capital investment.

Two issues are pertinent to highlight in relation to any shareholder and donor discussion on ramping up DFI and MDB investment to build back better. First, the IFC percentage of total assets invested to mobilise private investment has effectively remained the same since 2013 when it was 44.8%. Given that IFC has an 'extremely strong' capital adequacy position,[18] there is debate about whether the business model is overly conservative and whether IFC can materially ramp up its overall investment and/or its investment in high-risk markets without adversely affecting its credit rating. The new capital increase of $5.5 billion agreed in April 2018 to support IFC's 3.0 strategy, which aims to support more high-risk investment in IDA-eligible countries and fragile and conflict-affected states, will help in this regard. This observation is not unique to IFC and applies to several other MDBs (Attridge and Engen, 2019). Second, CDC's percentage of total assets invested in 2018 was lower than in 2013 when 84% of its total assets were invested to mobilise private finance. This is most likely explained by CDC's capital injection by the UK government and the time it takes to significantly ramp up investment pace in challenging markets in Africa and South Asia.

All of this is to acknowledge that calls to increase DFI and MDB investment must recognise these differences. Short of changing the operational structures of DFIs and MDBs, increases in investment are likely to be tightly correlated to increased capitalisations, albeit with a time lag – an unlikely scenario for the near future as government budgets are under stress due to responding to the Covid-19 crisis. How DFIs and MDBs can alter their operational structures to increase the amount they invest is outside the scope of this analysis but is an area of important future research.

4.2 Regional investment trends

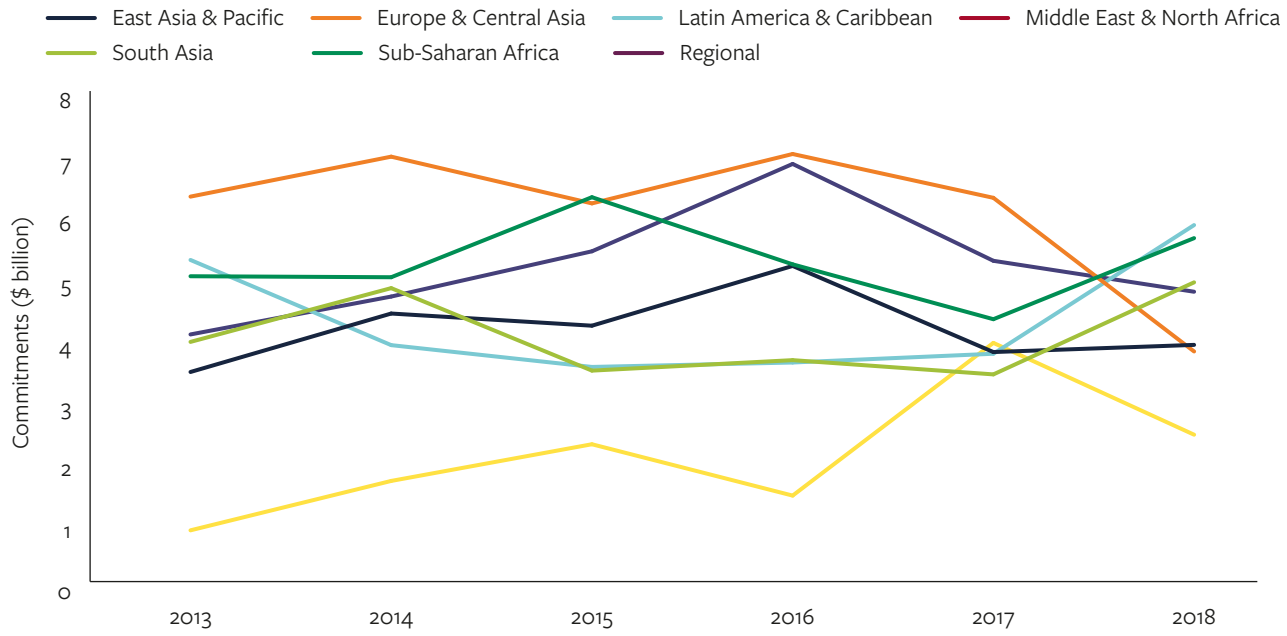
As highlighted in Chapter 2, the growth in net ODA and FDI flows have not been distributed evenly amongst the regions. From Figure 7, it is evident that this scenario also holds true for DFI and MDB investment. While every region except for Europe & Central Asia benefited from more investment in 2018 than it did in 2013, these increases were uneven. DFI and MDB investments in the Middle East & North Africa grew at a pace of 23.4% per year, largely due to increases in investment in Egypt and Tunisia after the Arab Spring and significant investments in Lebanon in 2017 and 2018. DFI investment growth in SSA and Latin America & Caribbean was more modest; 2.4% per year and 2.1% per year, respectively.

The most significant decrease in DFI and MDB investment was experienced by Europe & Central Asia as 2018 levels were 60% of its 2013 levels. Most of this decrease came in 2018 and was largely due to less annual investment in Turkey as 2018 levels were $3.2 billion less than the highest level reached in 2016.

The decrease in investment in 2018 significantly diminished Europe & Central Asia's dominant position as the region benefiting the most from DFI and MDB investment. In 2013, this region attracted 22 cents of every dollar invested; in 2018, it was 12 cents. This loss in share can mostly be explained as a result of the Middle East & North Africa increasing its share by 5% over the same period, as well as South Asia increasing its share by 2.2%.

18 Defined by Standard & Poor as risk-adjusted capital ratio above 23%. In 2018, IFC's risk-adjusted capital was 32% (S&P Global Ratings, 2019).

Figure 7 Annual mobilising commitments, by region, 2013–2018



Source: Authors' calculations based on the ODI dataset

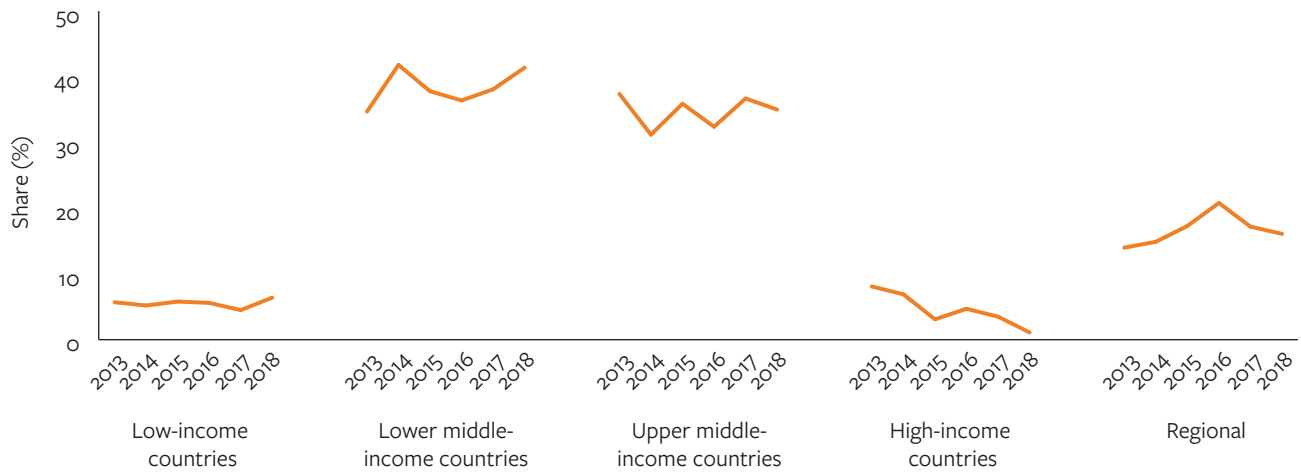
Given that FDI to SSA was decreasing significantly over the 2013–2018 period, the increase in annual DFI and MDB investment naturally brings forth the discussion regarding the ability of DFIs and MDBs to invest countercyclically. From 2013 to 2018, annual DFI and MDB investment to SSA grew by almost $620 million (12.5%); FDI inflows fell by $4.1 billion (10.2%) over that same time period. Simply, DFIs and MDBs do not have the balance sheet to fully offset these massive shifts in FDI flows. Further, it is important to understand the nature of these FDI flows to nuance this idea. UNCTAD (2020b) noted that much of the decrease in FDI inflows to SSA was due to lower world prices for commodities and fewer FDI inflows into extractive sectors. It is explained below in Section 4.5 that DFIs and MDBs have significantly scaled down their investments in extractive sectors. Thus, DFIs and MDBs are supporting the non-extractive sectors in SSA as these sectors benefit from fewer FDI inflows than SSA commodity-related sectors.

The net effect of these shifts and what they mean for investment-related development in SSA countries is beyond the scope of this report, but it must be understood to conceptualise the ability of DFIs and MDBs to be countercyclical. This understanding is increasingly important as DFIs and MDBs aim to support current clients during the Covid-19 crisis and recovery, and while stakeholders call upon these institutions to invest countercyclically during this period. The likely reality is that DFIs and MDBs will disappoint in this regard. With most of their investment capital already committed and their balance sheets potentially under strain as the impacts of the Covid-19 crisis are felt in their existing portfolios, DFIs and MDBs would need new capitalisations to materially ramp up investment in new clients. Moreover, as seen in the case of SSA investment, new investment may not go to sectors that have seen private sector retrenchment. All these factors must be taken into consideration as stakeholders discuss DFIs acting countercyclically.

4.3 Country income group trends[19]

As can be seen from Figure 1, the share of DFI and MDB investment going to LICs is broadly commensurate with the relative shares for which these countries account of total developing country GDP and total developing country FDI inflows. However, FDI has been decreasing in LICs (Chapter 3) and it would be expected that DFIs and MDBs, in their dual roles as investor and mobiliser, are viewed as part of the solution to this issue. However, there has been little shift in country income allocation of DFI and MDB investment (Figure 8). In 2013, LICs welcomed 5.7% of commitments; in 2018, it was 6.4% of commitments, an increase of $340 million in annual investments. With the $11 billion decline in annual FDI inflows over the same period, it is evident that the small shift in DFI and MDB investment allocation to LICs is far from filling this enormous gap. While the discussion above highlighted why DFIs and MDBs should not have been expected to fill this entire gap, they are expected to play a countercyclical role.

Figure 8 Share of mobilising commitments, by country income group, 2013–2018



Source: Authors' calculations based on the ODI dataset

19 As mentioned in Appendix 1, World Bank country income classifications were used to classify countries that received DFI investment and welcomed mobilised private finance. The income classification at the time of investment was used. Given that some countries were reclassified during 2013–2018, two projects in the same country (but at different times) can thus have different income classifications. The period during which this movement may be most pronounced is 2013 to 2014, when some large LICs graduated to lower middle-income status. These countries are Bangladesh, Kenya and Myanmar, which accounted for 3.6% of all DFI mobilising commitments in 2013 and 3.9% in 2014. The movement of these countries partially explains the decrease in LICs as a share of total DFI investment from 2013 to 2014 and the significant increase in share to LMICs. As these three countries accounted for 58% of DFI investment in LICs in 2013, it is noteworthy that investment to LICs did not decrease nearly as much in 2014, indicating that DFIs increased commitments to the countries that remained low income.

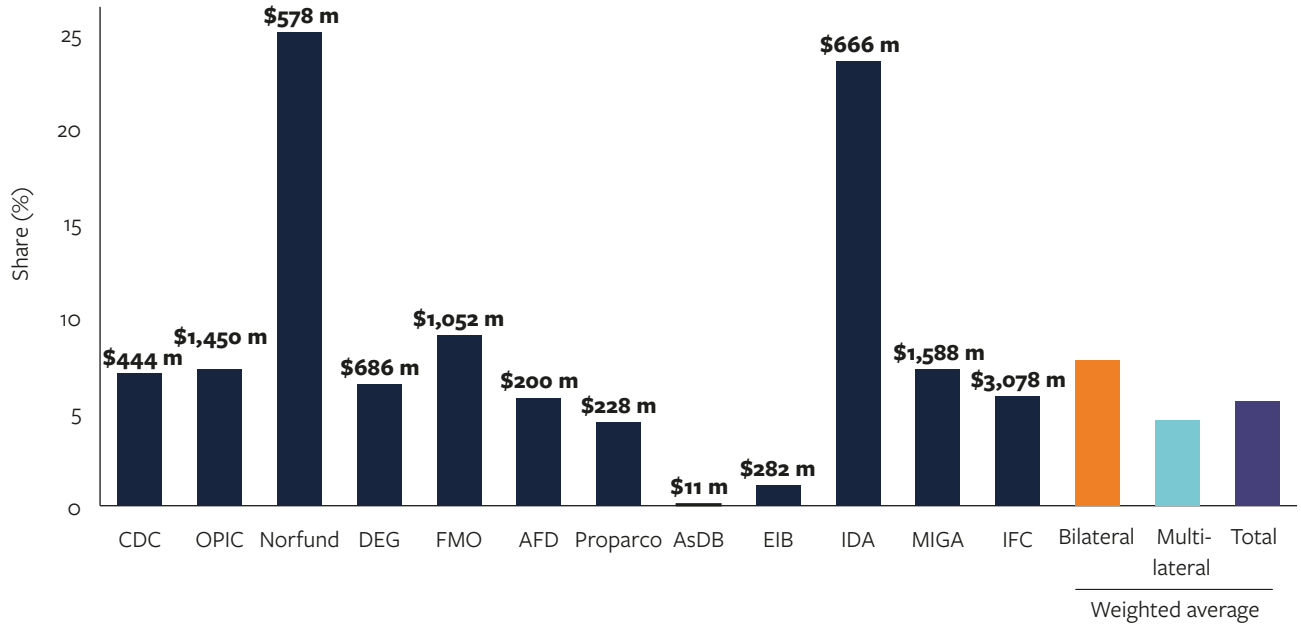
Any discussion of DFI and MDB investment in LICs must recognise that the ability to invest depends, in part, on their risk appetite. This appetite, for institutions that are funded by the international capital markets is constrained by the need to maintain an 'AAA' credit rating and the need for institutions not funded on the capital markets to remain financially sustainable and profitable. The discussion must also acknowledge the difficulty of the task given the constraints regarding the absorptive capacity of LICs to welcome investment. Two fundamental issues affect this demand side of the equation: (1) weak enabling environments and poor investment climates, and (2) lack of near investable commercial opportunities. DFIs and MDBs cannot fix the first issue but they are well placed to address the second. DFI and MDB investment should focus more on building markets and creating investment opportunities (i.e. act as market makers) rather than acting as market takers who respond to investment opportunities – 'hoovering up' a limited supply of near investable deals. This points to a clear action agenda, which is discussed in Chapter 6. The focus here is on the supply of DFI capital and investment, which remains stubbornly low in LICs.

Figure 9 shows the share of the DFI and MDB portfolio invested in LICs and DFI and MDB total investment in LICs over the period 2013–2018. IFC, MIGA, OPIC and FMO are the four largest investors in LICs, having invested over $1 billion each during this period. It is also clear that DFIs and MDBs explicitly setting targets to invest in LICs in their mandate or organising principles invest a larger percentage of their portfolios in LICs. Norfund has set a portfolio target of 33% of its investments being in the least developed countries (LDCs), so it is unsurprising that its investment pattern aligns with this goal. Similarly, IDA's partial risk guarantees are targeted at IDA-only countries,[20] with a focus on fragile and conflict-affected states. What is also interesting to note is the higher bilateral weighted average of portfolio investment in LICs, which may support the observation of our previous analysis that bilateral DFIs have a higher risk appetite and more flexibility than multilateral and regional institutions due to their different financing structures and regulatory requirements (Attridge and Engen, 2019).

A push to increase LIC concentration in DFI and MDB investment portfolios may imply acceptance of lower risk-adjusted rates of return with possible implications for DFI and MDB funding. The headroom of DFIs and MDBs to increase this concentration and any associated changes to business models requires further research and understanding. In doing so it may be instructive to look at DFIs that focus much of their investment in these markets, such as Norfund. For example, an evaluation of Norfund revealed that the internal rate of return (IRR) of the investment commitments it made in the LDCs from 2007 to 2013 was 3.95%, higher than IRRs for investments made in LMICs and UMICs. Investments in these LDC countries accounted for over 39% of Norfund's commitments during this period (Gaia Consulting, 2015). Whilst there is not more recent disaggregated data available, Norfund has only reported one year (2014) of a portfolio-wide negative IRR as it has pursued the aggressive LDC portfolio target outlined above (Norfund, n.d.). Evidently, backed by a strong mandate from its owners, Norfund has built capacity to find profitable opportunities in the world's poorest countries while remaining financially viable. Given the expected decline of investment to these countries due to Covid-19, DFI and MDB investment can play an important role in changing perceptions by pioneering and creating markets, but this will require a more targeted and tailored effort and may require a recalibration of MDB and DFI business models.

20 IDA countries are both low income and lower middle income.

Figure 9 Share of and total mobilising commitments to low income countries, by DFI and MDB, 2013–2018



Source: Authors' calculations based on the ODI dataset

Turning to the rest of the data on income groups illustrated in Figure 8, there has been a relative reallocation of DFI and MDB investment away from UMICs. These countries, as a collective, welcomed approximately the same amount of investment in 2013 as they did in 2018, which translated to a decrease in the annual share of total investment from 37% to 35%. LMICs had their share of total investment increase from 35% to 41% over this same period, while investments classified as regional increased from 14% to 16%. Much of the increase in investment in LMICs can be attributed to significant increases in the amounts invested in Egypt, India, Vietnam and Ukraine, which are investment increases likely due to significant economic growth in India and Vietnam and due to political imperatives in Egypt and Ukraine.

4.4 A deeper look at DFI and MDB investment and host countries

Analysing DFI and MDB investments by country income group provides insight but can overlook some nuance given the breadth of the classifications.[21] Upon segmenting host developing countries into deciles based on their GNI per capita, it is apparent that an analysis of flows based on country income groups overlooks three important points.

First, there has been an overall reallocation in DFI and MDB investment from wealthier developing countries to poorer ones. In 2013, developing countries below the 50th percentile of GNI per capita income welcomed 38% of investment; in

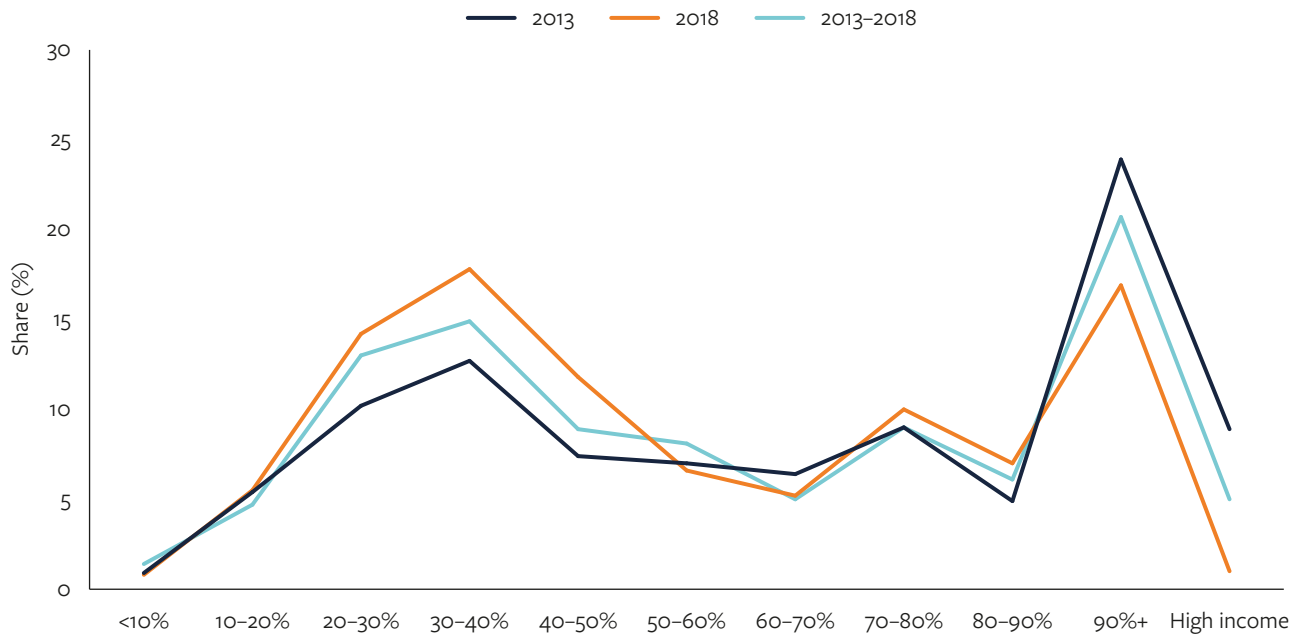
21 For example, as of July 2019, the World Bank classified LICs as having a gross national income (GNI) per capita below $1,026, LMICs having GNI per capita between $1,026 and $3,995, UMICs as having GNI per capita between $3,996 and $12,375 and high income countries as having GNI per capita over $12,375.

2018, it was 51%. As mentioned above, increased investment in India, Vietnam, Egypt and Ukraine is the main reason for this shift.

Second, developing countries that are almost classified as high income, above the 90th percentile of GNI per capita for developing countries, welcome a disproportionate amount of DFI and MDB investment.[22] DFI investment in Turkey and Brazil accounts for the majority of this investment. As Figure 10 shows, this share has decreased since 2013, but is nonetheless quite pronounced. Even among UMICs, developing countries at the top of the UMIC bracket are more apt to attract DFI and MDB investment than other UMICs. It is important to note that these figures are aggregated and do not reflect that 4 of the 12 sampled institutions have dedicated less than 3% of their commitments to countries in the 90th percentile of wealth.[23]

Third, the poorest of the LICs benefit from a negligible share of DFI and MDB investment. From 2013 to 2018, developing countries in the lowest income decile welcomed only 1.7% of investment. When countries in the low income group were discussed above, it was stated that investments in LICs accounted for 6.4% of commitments in 2018 – up from previous years and obfuscating that the poorest among these countries are welcoming less than 2 cents of every dollar invested by DFIs and MDBs.

Figure 10 Share of total DFI mobilising commitments based on beneficiary income decile



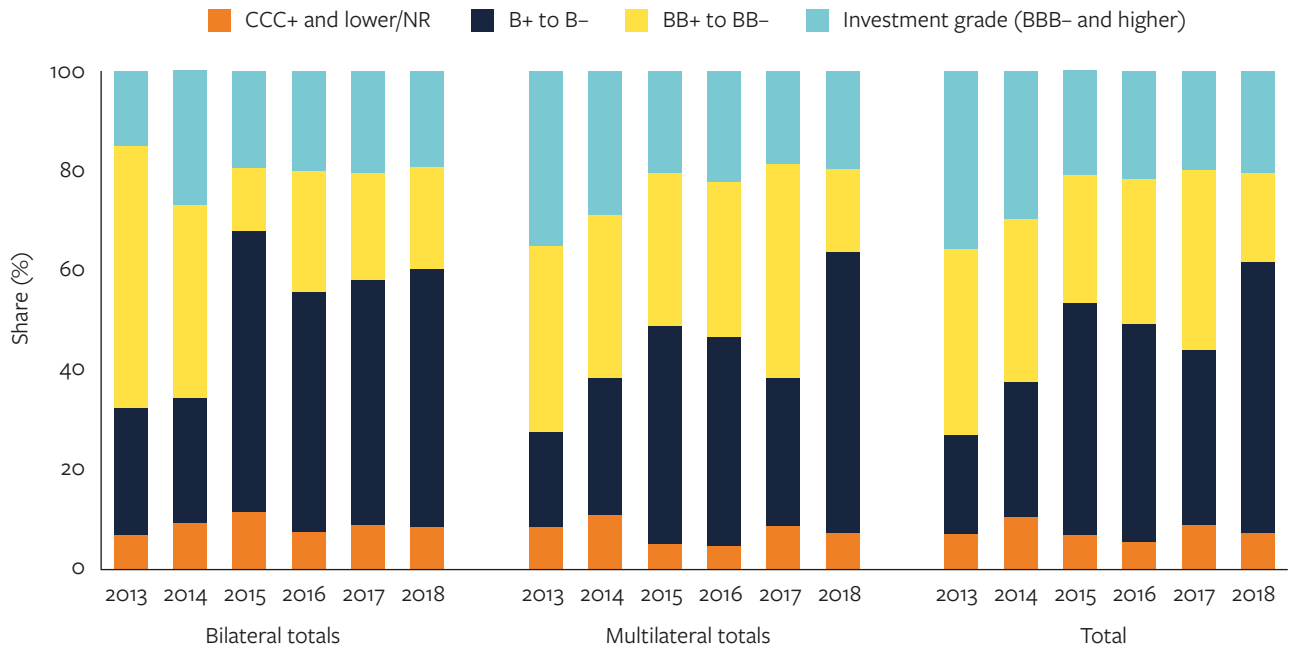
Source: Authors' calculations based on the ODI dataset

22 Only includes countries for which there was GNI per capita.
23 The four institutions are CDC Group, Norfund, AsDB and IDA.

As part of their mandate to mobilise, DFIs and MDBs will sometimes enter an investment as an anchor investor or co-investor to make the deal more 'investible' for other, preferably private, investors. These enhancements can take the form of 'hard' enhancements that can include subordinated loans, grant capital or risk management facilities, or can include 'soft' enhancements such as their preferred creditor status or their due diligence and ESG procedures that lower the risk to all investors and may enhance development outcomes. These enhancements are meant to alter the risk/return trade-off for private investors. To understand the willingness of DFIs and MDBs to pursue this mandate, one must understand the investment risks undertaken by these institutions. Unfortunately, specific data on how an individual investment is rated is not available in project databases, but investment risk can be proxied by using the sovereign risk rating of the country in which the investment is made. While acknowledging that most investments will have a riskier rating than the sovereign, the proxy does allow for some insight as to whether DFIs and MDBs are using their resources in deals that may already be investible or are more focused on making deals investible to other funders.

As illustrated in Figure 11 and taking the BBB rating as the threshold for an investment grade debt product, it is noteworthy that the share of total DFI and MDB investment into countries that have investment grade ratings has significantly decreased from 2013 to 2018. This decrease indicates that these institutions are increasingly willing to invest in countries, and deals, that are higher risk, a trend that is primarily driven by the multilateral institutions. This finding also chimes with the finding that there has been a reallocation of investment to countries with lower GNI per capita – unsurprising given that GNI per capita and sovereign ratings are correlated (Afonso, 2003).

Figure 11 Share of mobilising commitments, by beneficiary sovereign debt rating, 2013–2018



Source: Authors' calculations based on the ODI dataset

To the idea of mobilisation, it is worth noting that in 2018, 72% of the investments made by DFIs and MDBs were in countries that are within six notches of being investible (BB+ to B–). While there is not direct data that investments in these countries mobilised more private capital, it can be inferred that DFIs and MDBs use different instruments in these countries to accomplish this initiative. For example, 76.4% of all guarantees deployed by DFIs and MDBs were in countries that were rated between BB+ and B– and, from the OECD (2020b) report on private sector mobilisation, guarantees were reported as the financial instrument that mobilises the most private finance.

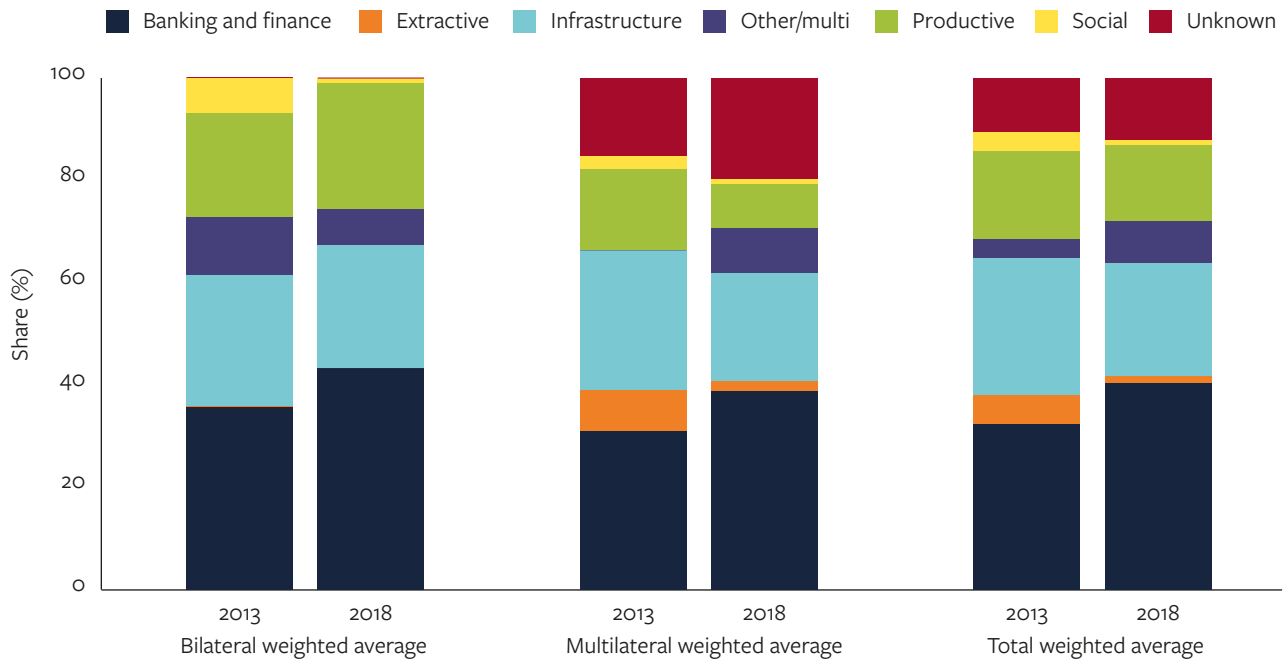
4.5 Commitments to sectors

With respect to the different sectors in which DFIs and MDBs invest, there are two main trends to note from Figure 12.[24] The first relates to the increase in investment in and through banking and finance, a trend reflected by both bilateral DFIs and MDBs. Anecdotally, most of this investment is provided for on-lending to certain segments of a country's private sector such as small and medium-sized enterprises (SMEs). The DFIs and MDBs tend not to offer much more clarification past this level of detail, so it is difficult to know how this 'banking and finance' investment is subdivided and on-lent amongst sectors. There has been greater recognition amongst DFIs and MDBs that investing via banking and financial institutions provides these institutions with the opportunity to support smaller ticket size investment. In effect, the investing DFIs and MDBs share the cost of due diligence with the financial institutions they are funding; institutions that have far better understanding of the local customer base and local economic environment. Still, these investments in financial institutions likely require greater monitoring on behalf of DFIs and MDBs to ensure that the financial institutions are fulfilling the mandate of the investment; a mandate that may be related to specific policy themes or international objectives, certain sectors, size of enterprise, or the economic empowerment of women, youth or marginalised persons.

The second trend to note from Figure 12 is the relative decline of DFI and MDB investment in the extractive sectors and in infrastructure. DFIs and MDBs do not want to be associated with investing in extractive sectors as many have reoriented their mandates to also include tackling climate change. In infrastructure, the decline is reflective of the change in investor sentiment and significant decline in private investment flows to the infrastructure sector in developing countries, which halved from an annual average of $150 billion in 2008–2014 to $75 billion since 2014 (Tyson, 2018). The bulk of the decline in DFI and MDB infrastructure investment is because of lower levels of infrastructure investment to UMICs, which in 2018 welcomed only 74% of the DFI and MDB investment they did in 2013.

24 How sectors are coded and consolidated is outlined in Appendix 1.

Figure 12 Sector shares of total mobilising commitments, 2013 and 2018

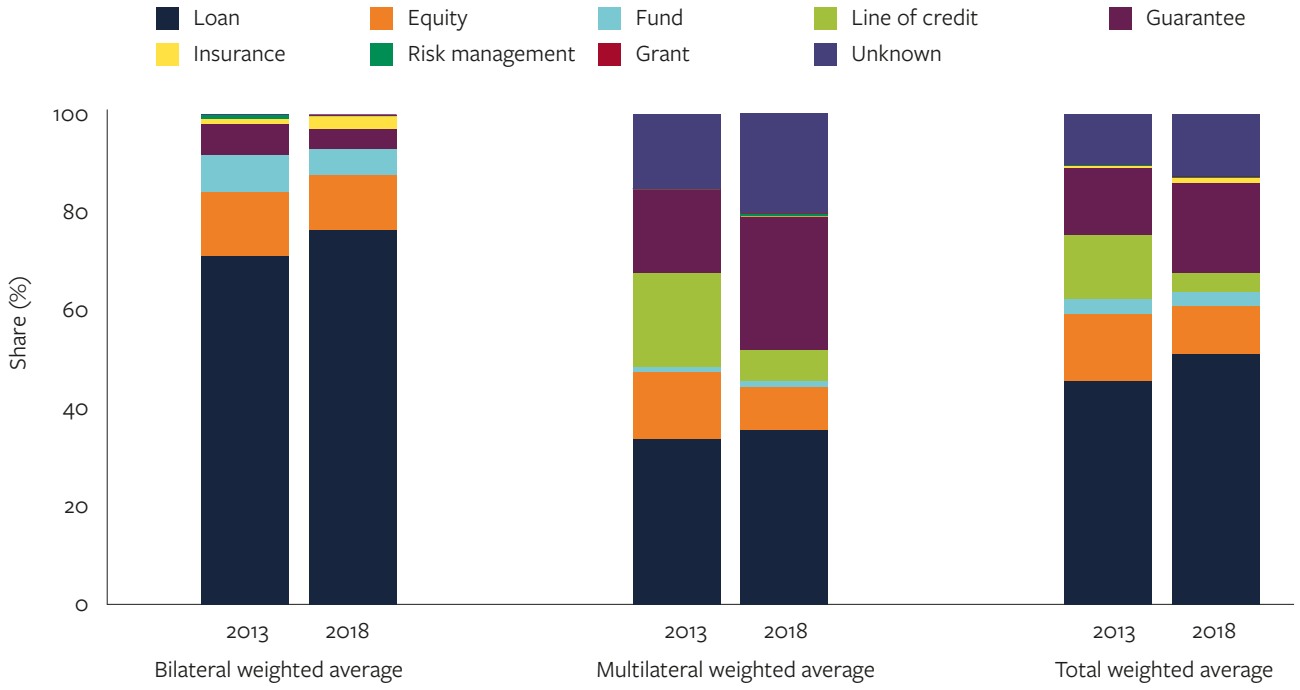


Source: Authors' calculations based on the ODI dataset

4.6 Commitments by financial instrument

Loans continue to dominate as the financial instrument of choice by DFIs and MDBs, and their deployment has increased overall. In 2018, over 76% of bilateral DFI commitment volumes were in the form of loans, up from 71.1% in 2013, and loans accounted for more than 51% of total DFI and MDB commitments in 2018, up from 45.6% in 2013 (Figure 13). Unfortunately, the collected data does not allow for examination of where these loans sit in the capital structure of each deal. MDBs and DFIs provide risk capital across the three risk levels in the capital structure of an investment, from equity at the bottom of the capital stack, which carries the most risk, through to mezzanine finance (e.g. preferred equity, convertible grants and loans, subordinated debt), through to senior debt at the top of the capital stack, which carries the least risk. These instruments all have different risk and return characteristics with different propensities to mobilise private finance depending on country and market context. Further, loans tend to be simpler to manage than other instruments and allow DFIs and MDBs to recycle capital more frequently. Although we do not have data on whether these loans are senior or subordinated, it is instructive to look at the instrument composition of blended concessional finance reported by DFIs and MDBs (DFI Working Group, 2019). External concessional resource is used by DFIs and MDBs to enable them to make investments that their own account balance sheet and pricing would not allow; it enables the DFI and MDB to take on more investment risk. 61% of this concessional high-risk bearing capital was deployed using loan instruments in 2018, 60% of which was in the form of senior debt (DFI Working Group, 2019). Given that this high-risk concessional capital is heavily deployed in the form of senior loans, it is reasonable to suppose that much of DFI and MDB own account loan investment takes the form of senior debt.

Figure 13 Instrument shares of total mobilising commitments, 2013 and 2018



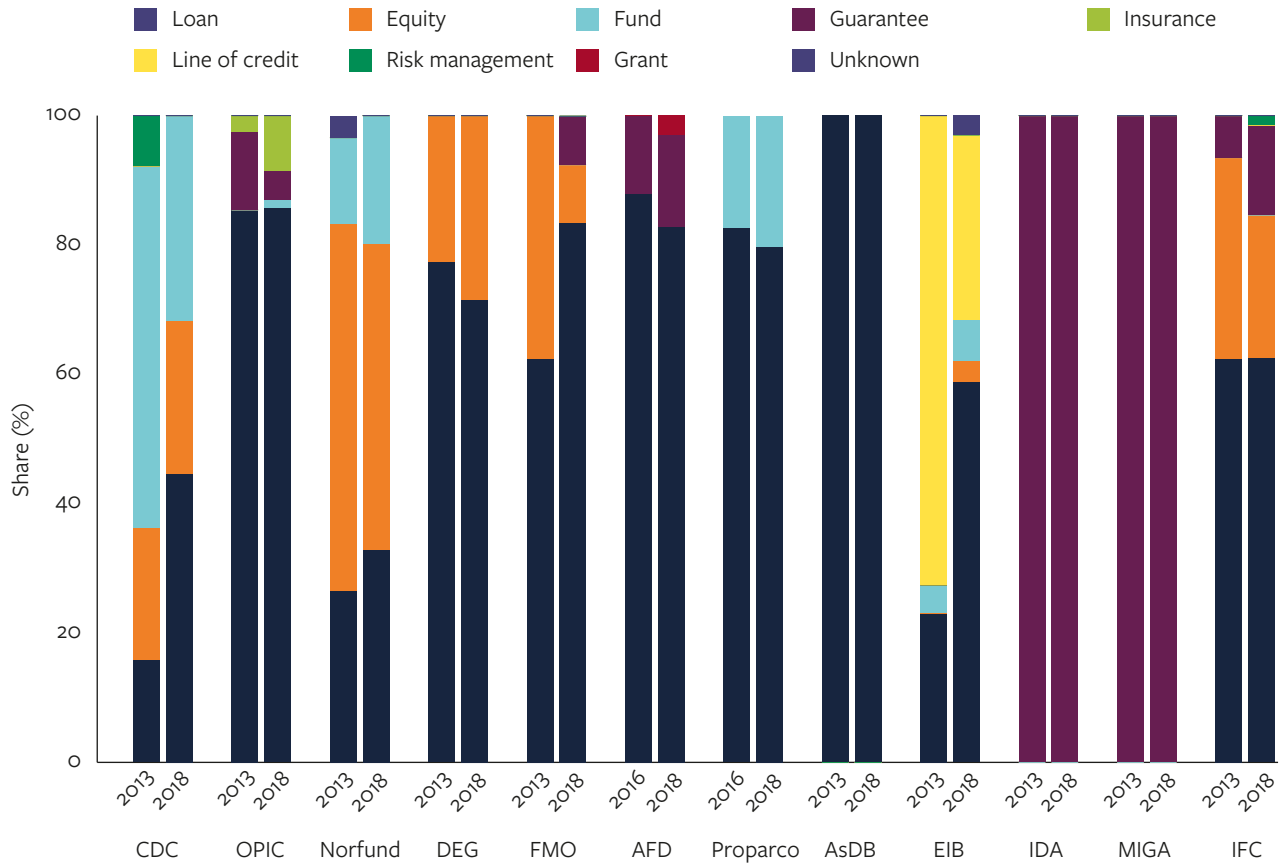
Source: Authors' calculations based on the ODI dataset

As mentioned above, guarantees[25] deployed by DFIs and MDBs mobilised the most private finance; however, their use remains limited overall and, as can be seen from Figure 14, the extent of their deployment varies by institution. It is noteworthy that while guarantees are used exclusively by MIGA and the included investments from IDA, they are used far less by other multilateral institutions and bilateral DFIs (Figure 14).[26] A number of factors are often cited for their limited use. Factors on the supply side include that they are counted in the same way as loans against the capital structure of DFIs and MDBs but are much more complicated and time consuming to negotiate, as well as the varied operational capacities among these institutions (Humphrey and Prizzon, 2014). On the demand side, transaction costs are higher than debt finance, and private investors find the DFI and MDB products to be too complex and the processes too slow and bureaucratic (Lee, 2017). There is much interest in ramping up the use of guarantees to mobilise private investment; however, further evidence is required to understand their efficacy. A recent analysis by Convergence finds that guarantees have been effective for mobilising commercial bank and corporate investment into infrastructure projects but have not yet effectively mobilised institutional investment at scale. A stronger evidence base is needed to help inform their effective use (Convergence, 2019).

25 Guarantees are accounted for based on the amount of a loan guaranteed by the institution in the year the guarantee was issued.

26 Note, IDA's guarantees refer to their partial risk guarantees in support of private investment. They exclude the IDA private sector window, which are counted in MIGA or IFC commitments to avoid double counting.

Figure 14 Instrument shares of mobilising commitments, by DFI and MDB, 2013 and 2018



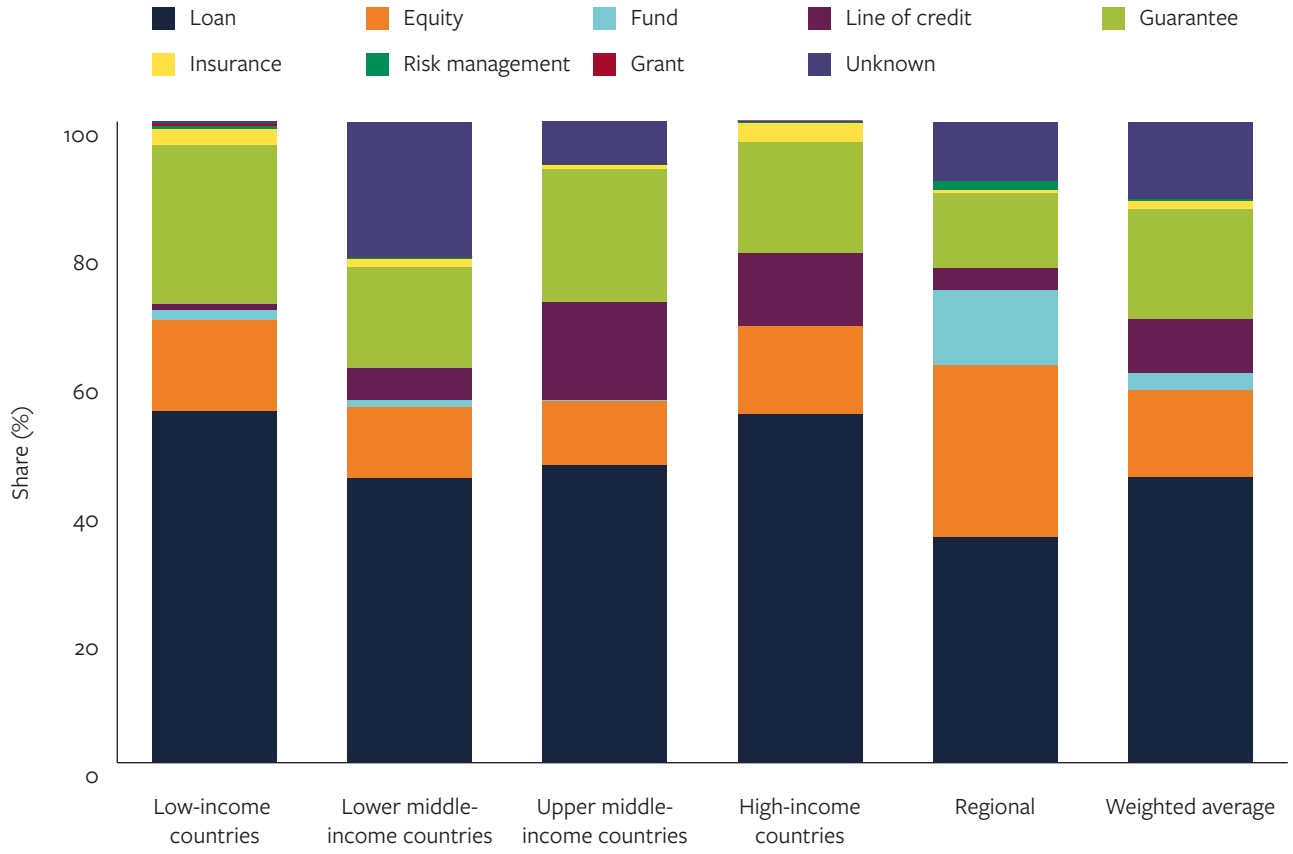
Source: Authors' calculations based on the ODI dataset

Another noticeable observation is the limited use of equity and the small decline of direct equity and fund investment (i.e. indirect equity investment) in the overall instrument mix of DFI and MDB portfolios, from 16.8% in 2013 to 12.6% in 2018. Only a relatively small number of DFIs and MDBs deploy equity capital. In terms of portfolio share in 2018, the leading DFIs are Norfund (67.2%), CDC (55.4%), DEG (28.4%) and IFC (22%), although the equity share of these DFI and MDB portfolios has decreased for CDC, Norfund and IFC. This has been most noticeable for CDC, who have materially switched the instrument composition to include more debt, and for FMO, whose equity share declined from 37.6% in 2013 to 8.9% in 2018. This trend is of concern given the relative scarcity and development additionality of equity investment, bearing in mind that equity markets are less developed than debt markets in many developing countries. DFIs and MDBs that have developed this capability should develop this further rather than retrench from it. That said, it must be acknowledged that equity is very different from debt in terms of the business models of DFIs and MDBs. Equity investment is riskier than debt: returns can be higher but much more volatile, and it ties up capital for long periods of time before return is potentially realised, with limited opportunities to exit. Further, equity investment is resource-intensive and it requires specialist expertise, which many DFIs and MDBs do not necessarily have.

Finally, Figure 15 illustrates how the mandates of the different DFIs and MDBs, and the instruments

they use, alters the country income breakdowns. For example, Norfund, because it usually invests via equity quite extensively and has a focus on LICs, accounted for 23 cents of every dollar of equity invested in LICs over the 2013–2018 period. The included investments from IDA and MIGA combined to account for 89% of guarantees issued for investments in LICs. Interestingly, as covered more thoroughly in Chapter 6, LICs and UMICs had the highest leverage ratios and, as seen in Figure 15, were the beneficiary countries which welcomed the most guaranteed investment on a proportional basis.

Figure 15 Instrument shares of mobilising commitments, by country income group, 2013–2018



Source: Authors' calculations based on the ODI dataset

5 Mobilisation of private investment in developing countries

Key findings

- From a small base in 2012, the amount of private finance mobilised by DFI and MDB investment has been increasing year on year by 13% and is being driven by MDB investment. However, DFI and MDB investment is not mobilising private investment at scale.
- UMICs still attract more mobilised private finance than LMICs despite attracting fewer commitments.
- Although from a small base in 2012, amounts mobilised have increased at the fastest rate in LICs. When studied at income decile level, there is a reallocation in progress, with increased amounts of private finance mobilised to poorer countries compared with prior periods.

The OECD has been working on measuring and collecting data on the amounts mobilised from the private sector by official development finance since 2012, including on the amounts mobilised by MDB and DFI investment.[27] The OECD has been gracious in sharing some of their data for this analysis, but was unable to share all data provided to it by MDBs for the period 2016–2018 due to these institutions citing a need for confidentiality. For this period, we use direct MDB mobilisation data contained in the MDB joint reports on private finance mobilisation. This data is not disaggregated by sector, country or instrument, which limits detailed analysis. This is disappointing and indicates a step backward in progress towards more transparent DFI and MDB operations. It is also not obvious what confidentiality is breached by providing semi-aggregated mobilisation data.

5.1 Trends in total amounts mobilised by selected DFIs and MDBs

The amounts of private finance mobilised by the selected DFIs and MDBs has been increasing from 2015 to 2018 (Figure 16).[28] However, volumes are low – far below ODA volumes – and DFIs and MDBs are not mobilising private investment at scale. While unable to ascertain the rate of growth between 2012 and 2015, from the 2012–2015 averaged amount to 2018, the total amount mobilised grew at a rate of 13% annually from a tiny base. This growth was led by the amounts mobilised by the multilateral institutions, which grew at 14.3% annually, whereas amounts mobilised by bilateral DFIs grew at 10.1% annually. As noted in the previous chapter, total mobilising commitments from the selected DFIs and MDBs grew at a rate of 1.6%[29] from 2013 to 2018, which suggests that overall leverage rates are increasing. This increasing leverage is discussed further in Chapter 6 as the growth of the amounts mobilised by the multilaterals is further interrogated.

27 For an in-depth discussion of the OECD's methodology to capture the amount of private finance mobilised and how it differs from other methodologies, see Chapter 2 of Attridge and Engen (2019).

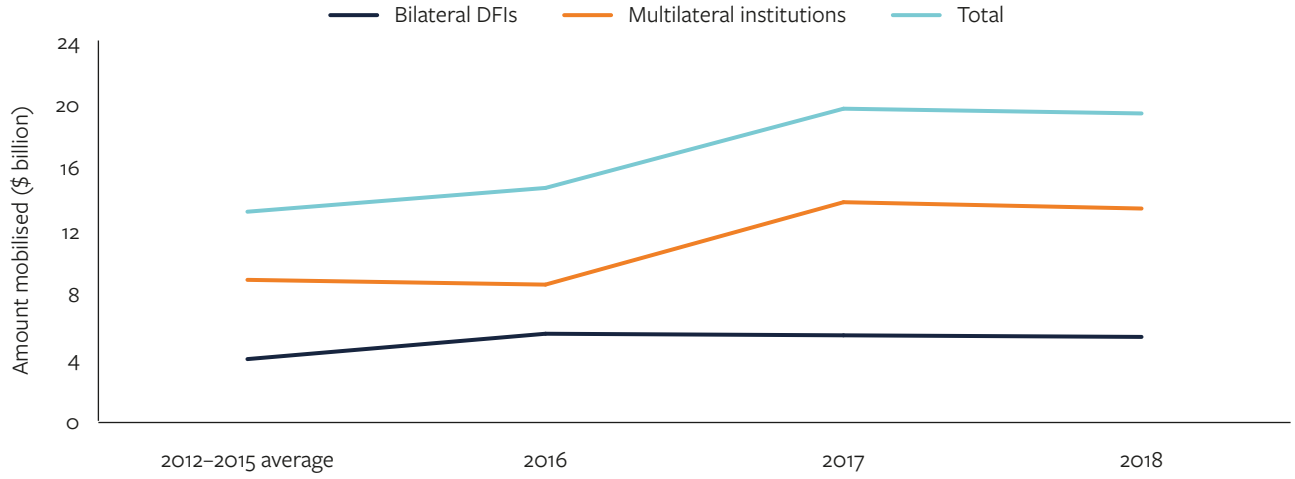
28 2019 MDB mobilisation data were published in January 2021 after this report had gone into publication. The data in the report show a continuation of this trend for our sampled MDBs in 2019. Private direct mobilisation for our sampled MDBs increased from $13.9 billion in 2018 to $15.2 billion in 2019, an increase of 8% (IFC, 2021).

29 DFI and MDB mobilising commitments for the selected DFIs excluding DEG, FMO and IDA actually declined at a rate of –0.1% annually.

5.2 Total amounts mobilised by region

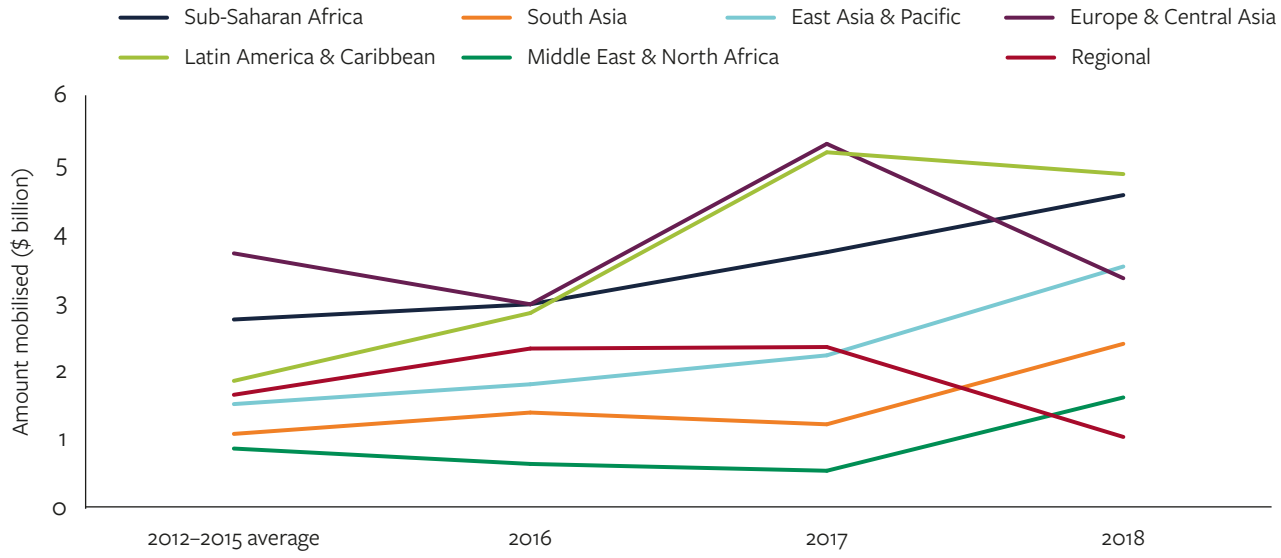
Before turning to Figure 17 and studying how DFIs and MDBs are mobilising capital in the different regions, it is important to note that the *Mobilization of private finance* report for multilateral institutions does not classify any of the mobilisation totals as regional.[30] Therefore, when the regional amounts decrease post-2015 it is because only the bilateral DFIs are classifying amounts mobilised as 'regional'.

Figure 16 Annual amount of private finance mobilised, 2012–2018



Source: Authors' calculations based on OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

Figure 17 Annual amount of private finance mobilised by region, 2012–2018



Source: Authors' calculations based on OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

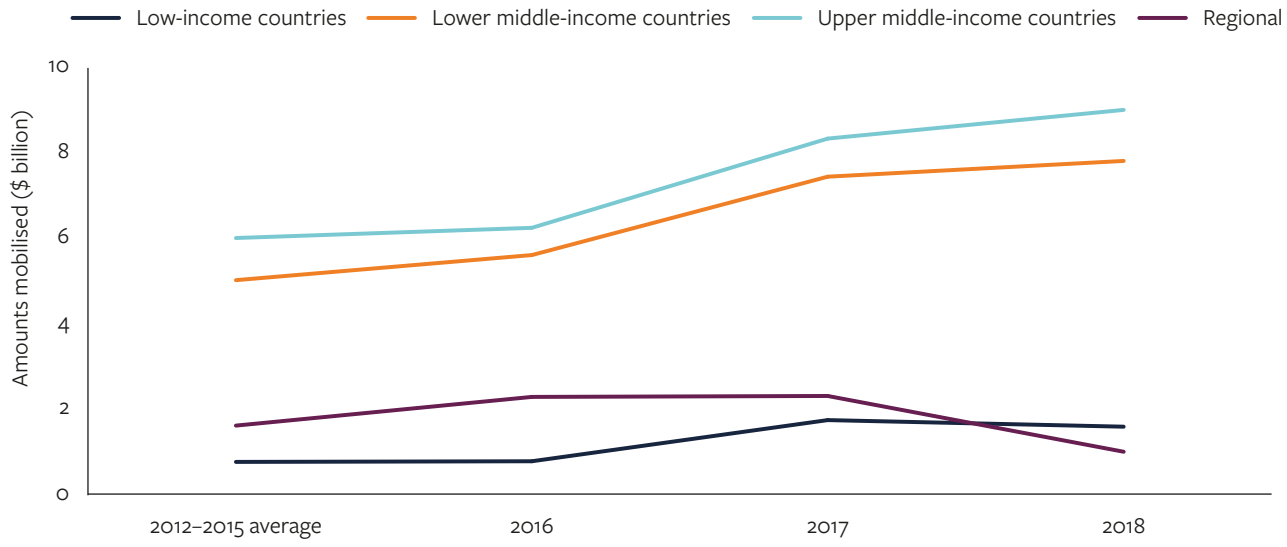
30 MDBs and DFIs invest regionally through collective investment vehicles (CIVs) that may span several regions. It is not clear how CIVs' cross-regional mobilisation is captured in the MDB *Mobilization of private finance* report.

Looking at Figure 17, it is noteworthy that all regions, except Europe & Central Asia, welcomed more mobilised private finance in 2018 than they had on an average annual basis from 2012 to 2015. On an amount basis, the largest gains for this time period were made by Latin America & Caribbean and East Asia & Pacific regions the respective annual amount mobilised of which grew over the time period by $3.0 billion (158% increase) and $2.0 billion (128% increase), respectively. Over that same stretch, amounts mobilised in SSA grew by $1.8 billion (65% increase) and amounts mobilised in South Asia increased by $1.3 billion (116% increase). Again, these figures are even more striking when compared with DFI and MDB investment commitment figures that showed more modest increases over the same period.

5.3 Trends in mobilisation by country income group

The concentration of private finance mobilised in LMICs and UMICs reflects the concentration of DFI and MDB commitments in these income groups. Interestingly, the amounts mobilised in UMICs are consistently higher than amounts mobilised in LMICs, but LMICs benefit from more investment, as documented in Chapter 4. On the face of it, this comparison implies that a dollar of DFI or MDB investment mobilises more private finance in UMICs than in LMICs, but may also imply that investments in LMICs require more investment from DFIs to attract private investment due to higher perceived risk. While likely that projects in UMICS have better credit ratings than projects in LMICs, it is also noteworthy that DFIs and MDBs employ guarantees and lines of credit more readily in UMICs (Figure 15). These higher leveraged products no doubt influence the mobilisation data in Figure 18.

Figure 18 Annual amounts mobilised by country income group by selected DFIs, 2012–2018



Source: Authors' calculations based on OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

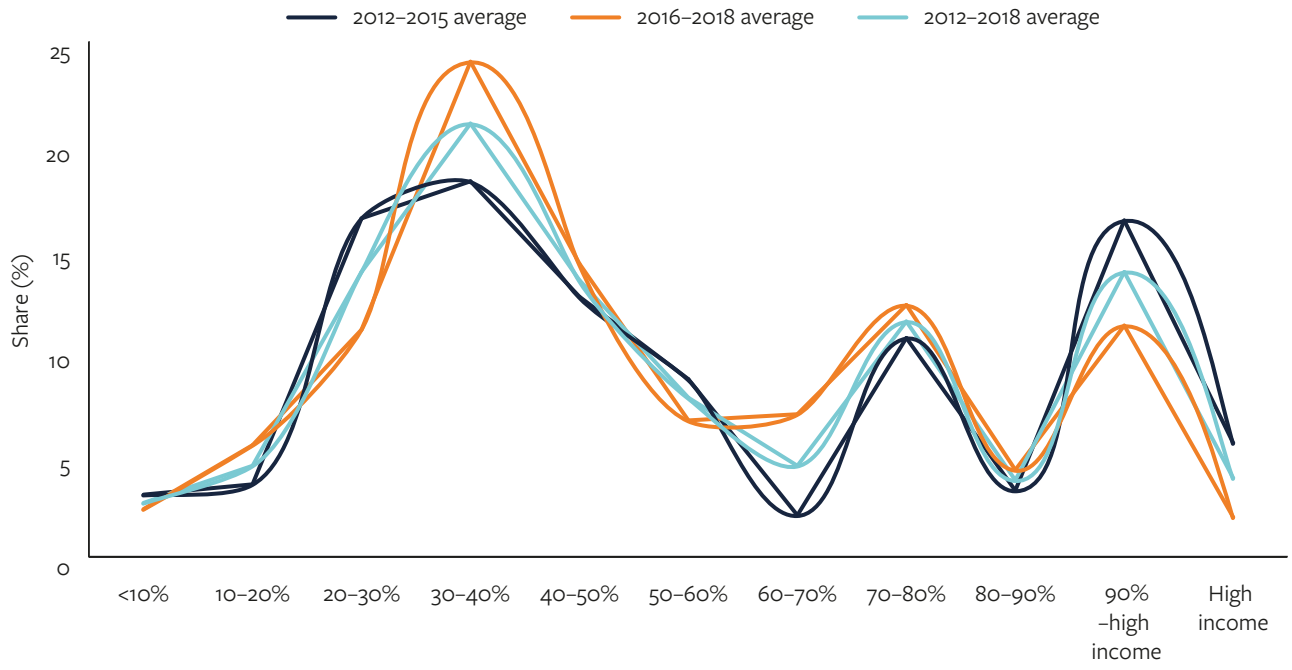
Among the income groups, amounts mobilised in LICs increased at a rate faster than the other income groups. LICs attracted 97% more mobilised private finance in 2018 than they did during the average year between 2012 and 2015. While this is impressive, the mobilisation data is aggregated so there is no way to determine whether this is an actual trend or based on one or two investments that occurred in 2017 and 2018 and attracted private investors.

5.4 A deeper look at amounts mobilised and beneficiary countries

As with the analysis on commitments, it is also informative to look deeper, past the income groups, to better ascertain which countries at which income levels benefit from more mobilised private finance than others. Given the lack of disaggregated data from the multilateral institutions for the 2012–2018 period, Figure 19 only captures amounts of private finance mobilised by the selected bilateral DFIs.

Nevertheless, Figure 19 is instructive in that it corroborates the findings that bilateral DFI commitment, and the private finance it mobilises, is moving down the income spectrum. As a share of total amounts mobilised by bilateral DFIs, developing countries in the top income decile (90% to high income) accounted for 16.3% of the 2012–2015 amounts; that share shrank to 11.2% in the 2016–2018 period. Conversely, the share of amounts mobilised by countries in the 30% decile rose by 5.8% between the two periods, an indication that bilateral DFIs, and their private sector partners, have become more willing to invest in LICs.

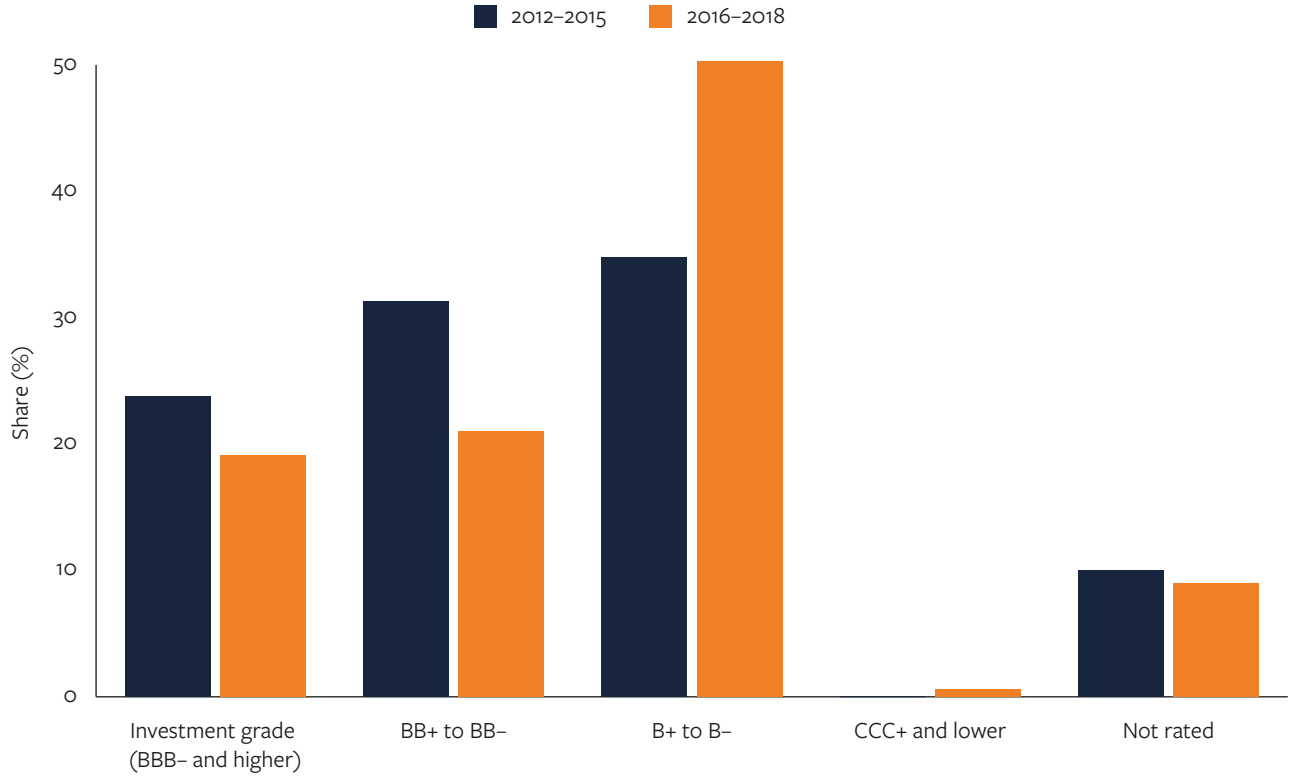
Figure 19 Share of amounts mobilised, bilateral DFIs, by beneficiary income decile, 2012–2018



Source: Authors' calculations based on OECD data

Unsurprisingly, the shift towards mobilising private finance in LICs coincided with a shift into countries that have higher sovereign risks, and likely, projects that are higher risk. As can be seen in Figure 20, during the 2012–2015 period, 23.8% of the amounts mobilised went to countries whose sovereign risk was considered investible (BBB– and higher); for 2016–2018 that share decreased to 19.1%. Even among the amounts mobilised in countries considered to have speculative grade sovereign debt (BB+ and lower), the comparison between the two time periods indicates that speculative grade investments were getting riskier, as the share of amounts mobilised in countries rated B+ to B– increased significantly. An exception to this trend towards riskier markets occurred as amounts mobilised to countries that do not have sovereign debt ratings declined over the two time periods; however, this decrease was 1% as a share of total amounts mobilised.

Figure 20 Share of amounts mobilised, bilateral DFIs, by beneficiary sovereign credit rating, 2012–2018



Source: Authors' calculations based on OECD data

6 Development finance institutions and multilateral development banks leverage ratios

Key findings

- Leverage ratios remain low overall and below one dollar, significantly less than what is needed to mobilise SDG investment at scale.
- However, overall leverage ratios have increased during the 2013–2018 period from 49 cents on the dollar to 69 cents on the dollar. Leverage ratios for bilateral DFIs are higher than MDBs, but MDB ratios appear to be increasing more quickly. Further study and data are required to fully understand what is driving this change.
- Overall, leverage has been highest in LICs, at 87 cents on the dollar, followed by UMICs (73 cents), then LMICs (60 cents).
- Investments in Latin America and the Caribbean region mobilise the most private finance per dollar of DFI investment, whereas regional investments mobilise the least.

With data on DFI and MDB investment and on the amounts of private finance mobilised by these institutions, leverage ratios can be calculated to understand how much private sector investment was mobilised per dollar of investment. It is interesting to look at leverage as this is often at the core of policy-makers' arguments for increasing investment in DFIs and MDBs and/or investing ODA to mobilise private finance. As noted in our previous work, the importance of leverage ratios should not be overstated. Further, these ratios should be approached with caution due to a number of interpretative issues: they do not imply causality or financial additionality; they say nothing about development additionality; and leverage can be calculated in different ways so measurement is problematic (Attridge and Engen, 2019).[31] The intention here is to anchor expectation about the potential of DFI and MDB investment to mobilise at scale and stimulate debate. Further research is needed to explore what leverage ratios could or should look like and hence how DFIs and MDBs are performing.

Before turning to the data, three key issues must be highlighted:

1. The amounts of private finance mobilised were self-reported by the sampled DFIs and MDBs.[32] They were not modified for this calculation. Due to the lack of available disaggregated mobilisation data we use different sources of data from the OECD and from MDBs. These datasets are underpinned by different methodologies, so caution should be taken as there is disagreement between the OECD and the MDBs on methodology, including

31 Assessment of financial and development additionality is complex and challenging, and is beyond the scope of this analysis.

32 For the reasons cited at the start of Chapter 5, DEG, FMO and IDA were not included in the Chapter 6 analysis.

the issue of double counting (Attridge and Engen, 2019). For the multilateral institutions in 2013–2015 we use the semi-aggregated OECD mobilisation figures. For 2016–2018, we use the private direct mobilisation reported by the multilateral institutions in their joint report (IFC, 2019), as OECD semi-aggregated data is not available for the confidentiality reasons mentioned above. For bilateral DFIs, we use the OECD mobilisation data. As noted in our previous work, the analysis is undertaken by way of illustration, to stimulate discussion and highlight the need for greater transparency to enable more precise analysis. It is the picture the data portray in the context of the SDG financing gap that is key, rather than the imprecise methodology used.

2. Commitment data was downloaded from project databases, checked for completeness against each institution's annual report, and then coded at the investment level to ascertain whether the investment is mobilising.[33] For some institutions, there is no way to discern whether an investment was mobilising or not, so, in those cases, it was included. However, only one of nine institutions included in the leverage analysis had all of their investment transactions classified as mobilised.[34] This means that there is a possibility of mobilising commitments being underreported in this analysis and our estimates may overestimate the actual leverage ratios.
3. The leverage ratios presented below differ slightly from those presented in our previous analysis (Attridge and Engen, 2019). These differences are the result of the inclusion of more institutions in this analysis and more data provided by the DFIs and MDBs than had been available previously. It must be underlined that these figures are iterative and subject to change if different data is provided; however, to date, these calculations present our best estimates of the efficacy of DFI and MDB investment to mobilise private finance. They are approximate figures that anchor discussion and illustrate the direction of travel.

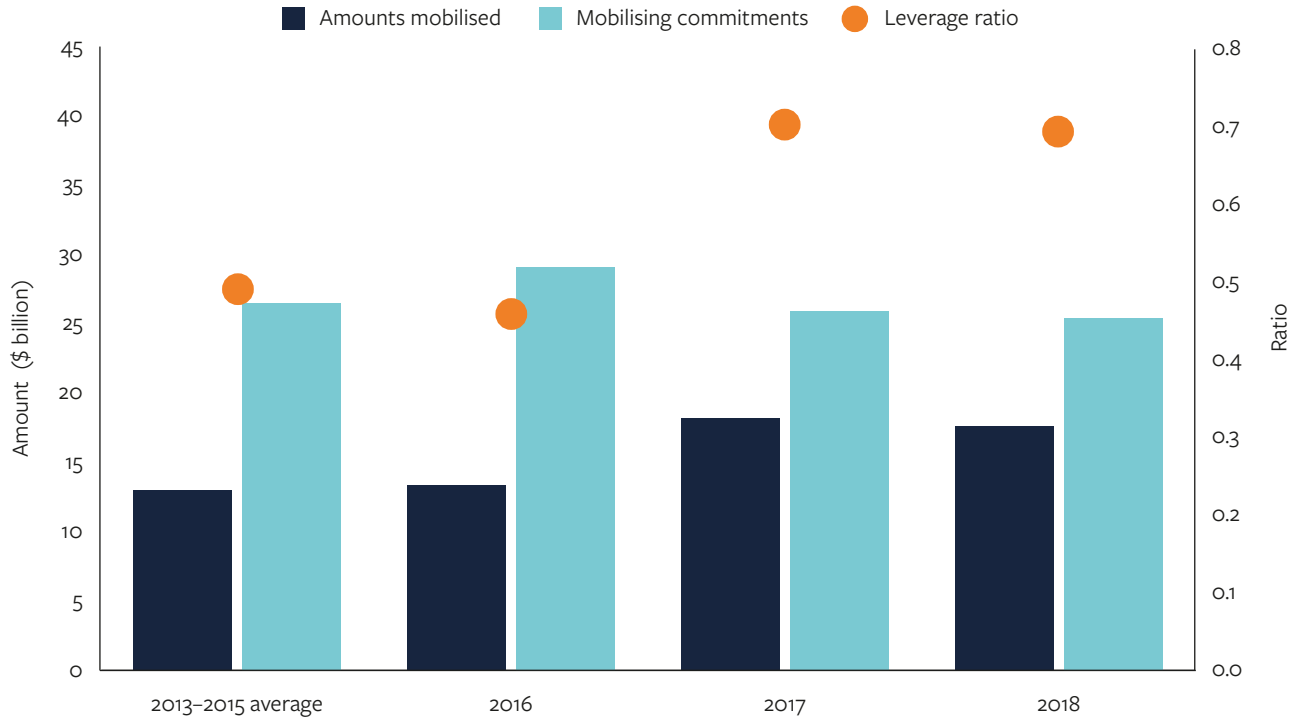
6.1 Total leverage ratio of selected DFIs and MDBs

Amounts mobilised by the selected DFIs and MDBs have been increasing faster than their mobilising commitments, resulting in an increasing leverage ratio (Figure 21). While the increase from 49 cents of private investment mobilised per dollar of investment during the 2013–2015 period to 69 cents in 2018 is a step in the right direction, it remains a far cry from what is needed to mobilise investment at scale to make a dent on the SDG funding gap. While it is important to recognise the progress made, DFIs and MDBs need to significantly improve their mobilisation efforts and leverage ratios if their investment is an important contributor to filling the funding gap. If not, expectations about these investments need to change.

33 Analyses of data completeness and classification of investments as mobilising can be found in Appendix 2 and Appendix 3.

34 For a deeper discussion of how investment commitments are classified, please see Appendix 1. Briefly, it is non-sovereign transactions where it was clear that the total project value was more than the DFI or MDB investment.This allows for the assumption that the other investment was private and mobilised by the DFI or MDB capital.

Figure 21 Total leverage ratios of selected DFIs and MDBs, 2013–2018



Source: Authors' calculations based on ODI dataset, OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

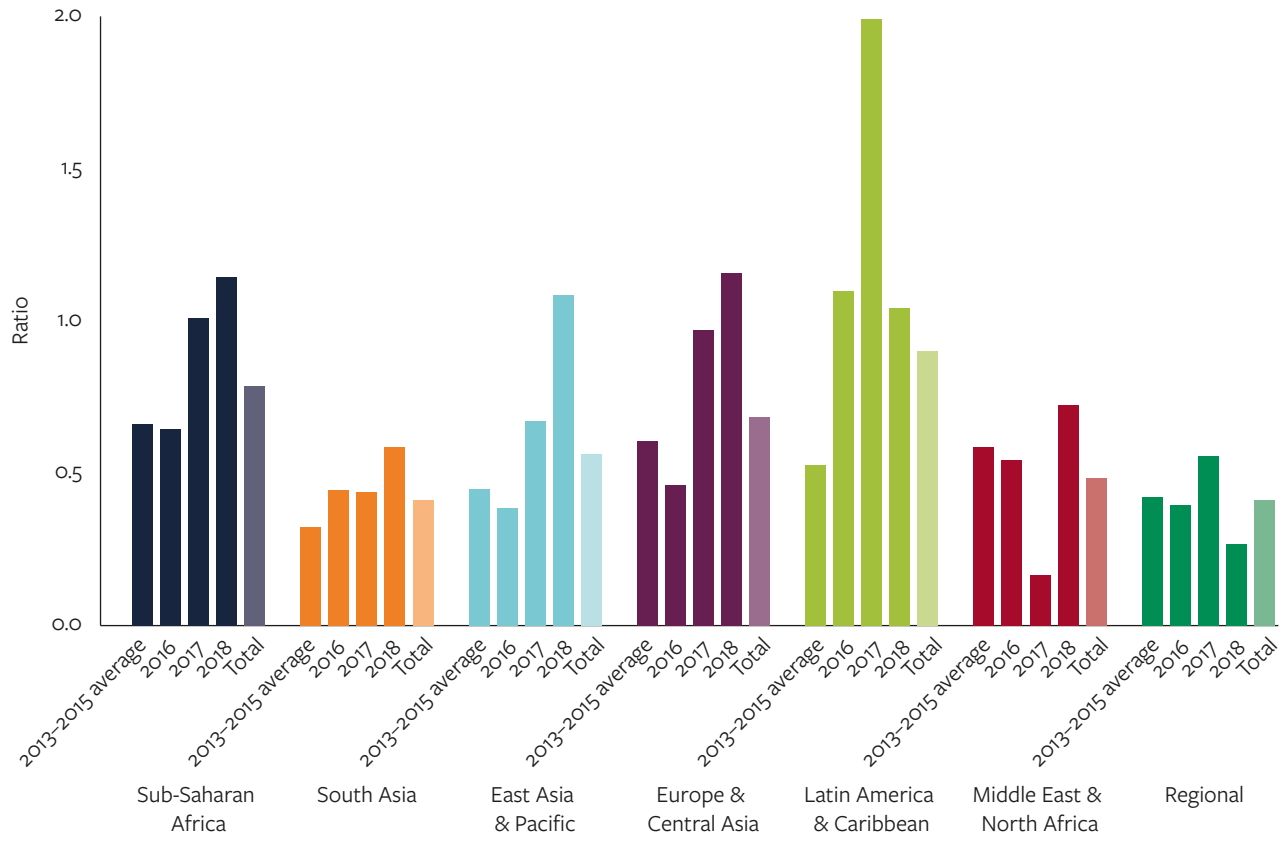
6.2 Regional leverage ratios

From a regional perspective, there have been across-the-board increases in the leverage ratios, except for DFI and MDB investments and amounts mobilised that are classified as regional. When compared with the leverage ratios based on the 2013–2015 average figures, regions that experienced the most substantial increases by 2018 included East Asia & Pacific (142% increase), Latin America & Caribbean (98% increase) and Europe & Central Asia (91% increase). Looking at the 2013–2018 period as a whole, DFI and MDB investments in Latin America & Caribbean and SSA were the most prolific regions in which to mobilise private finance, a surprising result when coupled with the fact that these two regions only benefited from an increase of 11.4% in commitments in 2018 than they did in 2013 (Figure 22).

6.3 Country income group leverage ratios

Leverage ratios are highest overall in LICs (Figure 23). This is surprising when considering that annual FDI inflows decreased significantly from 2013 to 2018, and DFI and MDB commitments increased only modestly. Nevertheless, it is impressive that the leverage ratio for investment in LICs increased by 58% from 2013–2015 averages to 2018 when commitments increased by less than 15% over that same period. As noted in Chapter 5, it is possible that these results are based on a few investments, so caution in interpreting these findings should be exercised.

Figure 22 Leverage ratios, by region, 2013–2018

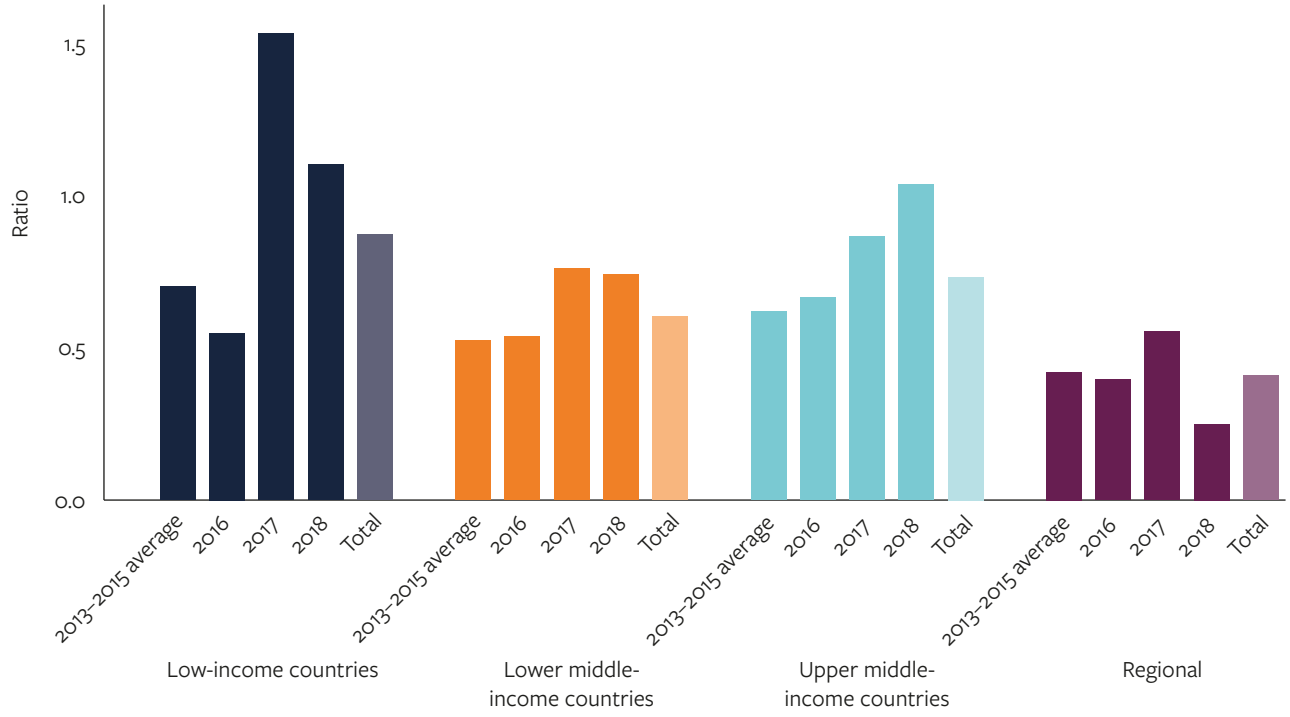


Source: Authors' calculations based on ODI dataset, OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

Although the marginal increase in the leverage ratios for LMICs and UMICs could be perceived as disappointing, it is important to put them into context with respect to the amounts that DFIs and MDBs invest in these countries. The increases in the leverage ratios of these two country income groups, when combined with the significant increase in commitments to these countries, translates to more mobilised private finance into these countries. For instance, if the leverage ratio for DFI and MDB investment in LMICs had remained constant from the 2013–2015 average of $0.52 rather than increasing to $0.74 in 2018, LMICs would have missed out on more than $2.3 billion in mobilised private finance in 2018. Under the same assumptions, UMICs would have missed out on $3.7 billion.

This issue brings up a path of research that will need to be undertaken in the future: to ascertain whether there is a ceiling to leverage ratios that is based on the income of a country. Theoretically, it is likely that as countries progress along the income spectrum, the gap-filling role of DFI and MDB investment will be supplanted by private investment. In those cases, it should be expected that DFI and MDB investment is negatively correlated with a country's income as these institutions pull back their operations. What this means for the behaviour of leverage ratios depends on the additionality of DFI and MDB investment in various contexts and is an area for further research.

Figure 23 Leverage ratios, by country income group, 2013–2018



Source: Authors' calculations based on ODI dataset, OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

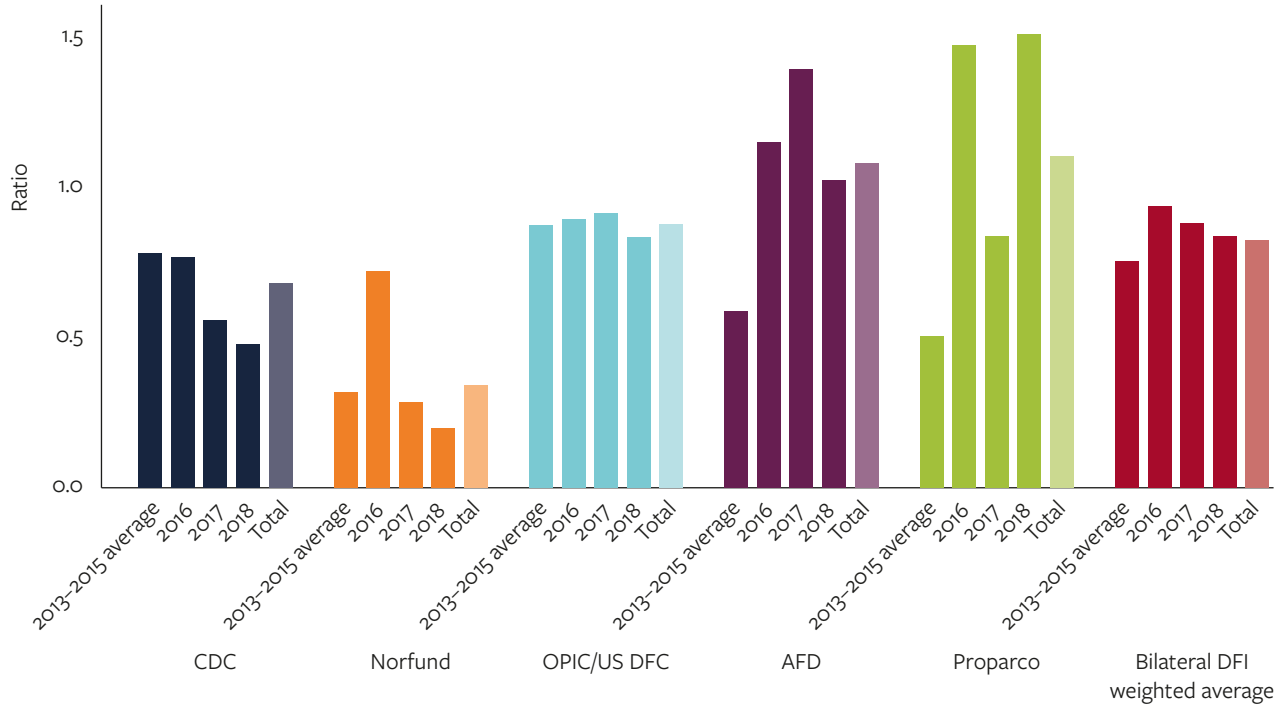
6.4 DFI and MDB leverage ratios

We calculate the leverage ratios for individual DFIs (Figures 24 and 25) and observe two important takeaways:

1. Leverage ratios calculated for the bilateral DFIs are less volatile than those of the multilateral institutions. While the weighted average leverage ratio of bilateral DFIs hovered between $0.75 and $0.95 over the 2013–2018 period, settling at $0.84 in 2018, the ratio of multilateral institutions was at a low point of $0.40 in 2016 and finished at $0.76 in 2018.[35] Deeper analysis of the data shows that the volatility of the multilateral ratios is largely a function of volatile reporting of amounts of private finance mobilised. During the period in which the multilaterals published their own amounts of private direct finance mobilised (from 2016 to 2018), the amounts they reported varied significantly.
2. Despite the volatility, the leverage ratio of the multilateral institutions is increasing while those of the bilateral DFIs are more static. This growth in the multilateral leverage ratio is mostly due to increases in the leverage ratio of IFC, while the consistency of the bilateral leverage ratio is mostly due to OPIC/US DFC being the most significant bilateral DFI and having a consistent leverage ratio from 2013 to 2018. As US DFC is enlarging its product offering to include equity, its own leverage ratio is expected to change, which will significantly impact the bilateral DFI weighted average leverage ratio in the future.

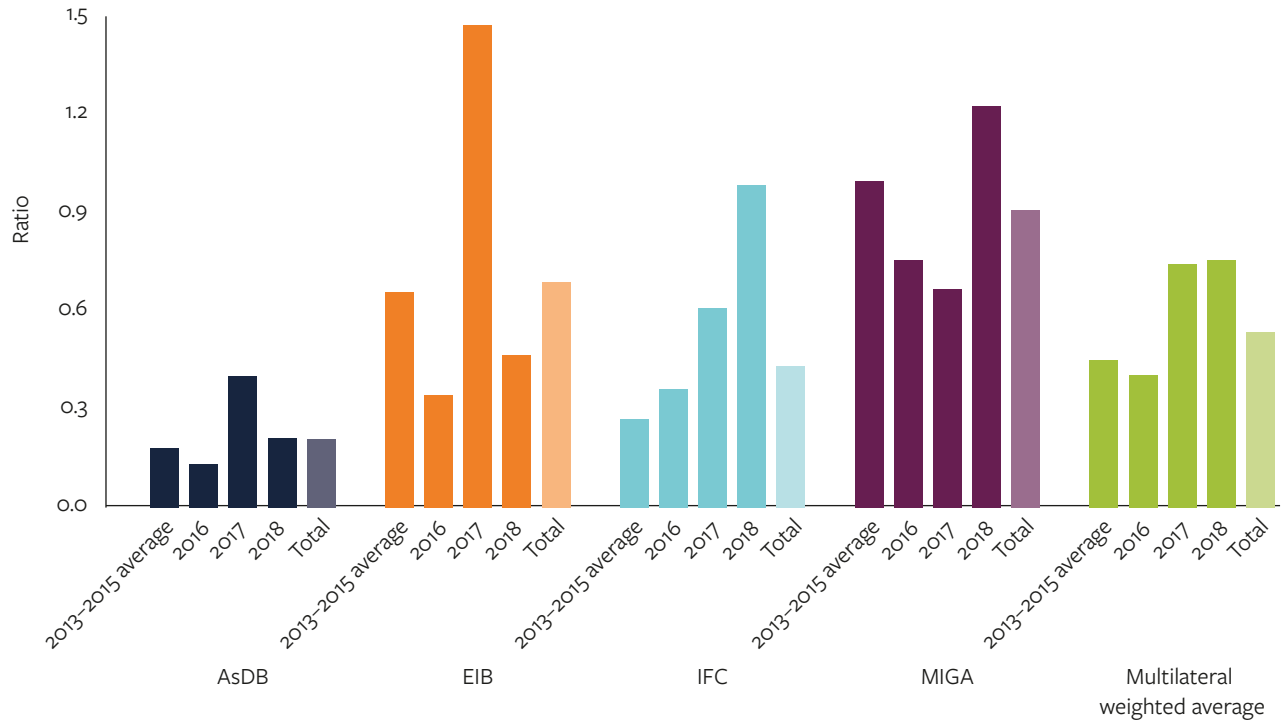
35 Note that AFD and Proparco leverage ratios may be overestimated as the data provided by AFD and Proparco investments is less than the figure in their annual reports.

Figure 24 Leverage ratios, by bilateral development finance institution, 2013–2018



Source: Authors' calculations based on ODI dataset and OECD data

Figure 25 Leverage ratios, by multilateral development bank, 2013–2018



Source: Authors' calculations based on ODI dataset, OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

6.5 Multilateral leverage ratios: a deeper look

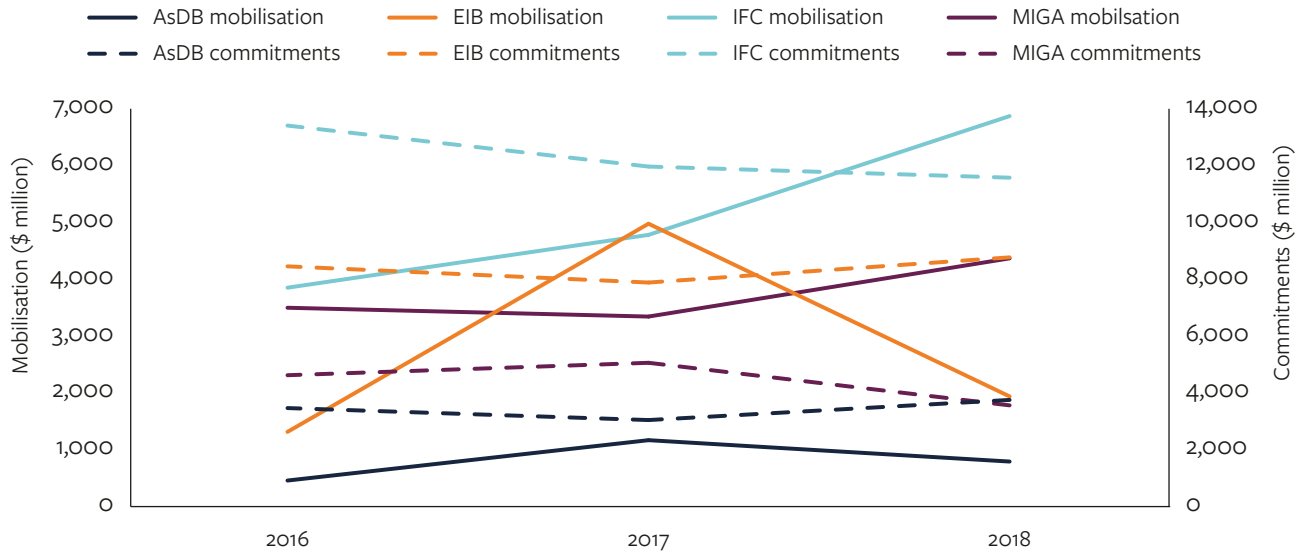
The multilateral weighted average leverage ratio decreased from the 2013–2015 average level to a lower level in 2016, then more than doubled from 2016 to 2018 (Figure 25). Given that the bilateral weighted average did not vary in the same way, it is necessary to do a deeper analysis on the multilateral leverage ratios to understand why.

The increased multilateral leverage ratio has been driven by increased amounts mobilised by IFC and MIGA, and a slight increase by EIB from 2016 to 2018 after mobilising an unusually large amount in 2017 (Figure 26). It is also important to note that the commitment amounts in Figure 26 are total commitments, not a smaller number of mobilising commitments. By presenting the data this way, there is no question as to how commitment classification may or may not be influencing the leverage ratios.

The most striking point from the data presented is that, for both IFC and MIGA, amounts mobilised increased significantly, whereas IFC's annual commitments and MIGA's annual exposure decreased, which is not what one would expect. Upon further investigation, it is evident that the share of IFC commitments increased to LICs (3% to 6% share) and LMICs (25% to 34% share), but the shifts accounted for an increase of less than $800 million from 2016 to 2018 in these two income groups. The share of guarantees employed by IFC increased by 5.5%, but equity decreased by 13%.

Conversely, MIGA's share of its commitments to UMICs increased by 30% and to LMICs decreased by 28%. An analysis of data on changes in allocation patterns to income group or instruments employed did not provide a clear, unequivocal answer as to why the amounts mobilised increased while commitments decreased. In light of the limited transparency on mobilisation data, this fuels a certain degree of scepticism. The issue was discussed with IFC who offered some potential explanations, including the use of unfunded risk transfers, which reduces the commitment on the balance sheet and increases leverage (Box 2). Further research on this issue would be valuable to help understand how new products are driving increases in mobilisation and leverage.

Figure 26 Multilateral institution amounts mobilised and total commitments, 2016–2018



Source: Authors' calculations based on ODI dataset, OECD data and MDB *Mobilization of private finance* report (IFC, 2019)

Box 2 Increased mobilisation by International Finance Corporation

An increase in the amount of private finance mobilised by IFC is the largest contributor to the increase in the weighted leverage ratio of multilateral investments. Upon consultation with IFC, it was noted that these higher mobilisation numbers may be due to the success of IFC Asset Management Company (AMC) as a platform to leverage IFC equity investments, the growth of IFC's Managed Co-Lending Portfolio Program (MCPP) and the new use of unfunded risk transfers.

IFC AMC, created in 2009, invests in a separately managed pool of funds that usually co-invests equity alongside IFC. In some cases, this allows IFC to reach beyond its investment limits and may also allow an investee to access IFC AMC equity for investments in which IFC would prefer to provide debt. As a separately managed fund, IFC AMC counts the establishment of its thematic funds with other investors as mobilisation, as well as the mobilisation that flows from individual investments from the thematic funds. As a mature strategy, the mobilisation by IFC AMC accounted for between 2% and 7% of the IFC's annual reported mobilisation from 2016 to 2018, according to its annual reports.

The most likely cause of the significant uptick in mobilisation rate is due to the MCPP. The MCPP builds a loan portfolio for an investor that mirrors the portfolio IFC is creating for its own account – similar to an index fund. MCPP investors and IFC sign upfront administration agreements determining the makeup of the portfolio based on agreed eligibility. Investors pledge capital upfront and then as IFC identifies eligible deals, investor exposure is allocated alongside IFC's own per the terms of the agreement. Although the MCPP has been around since 2013, it took on seven of its eight institutional investors in 2017 and 2018. For example, in 2018 alone, AXA and Swiss Re agreed to invest $500 million each in MCPP. As of 2018, MCPP had raised $7 billion from eight global investors.

Like IFC AMC, MCPP counts the original contribution of investors into the platform as mobilisation but also counts private investment in follow-on IFC project investments in which MCPP funds are deployed. IFC reported that syndicated loan mobilisation (including MCPP) increased from $5.4 billion in 2016 to $7.7 billion in 2018 (66% of mobilisation reported in the IFC Annual Report). IFC disclosed in the MDB *Mobilization of private finance* reports that its mobilisation has increased by $3 billion over that same period, so it is likely that the majority of this increase came due to the institutional investor funding of MCPP.

Finally, IFC has started to use unfunded risk transfers that access a hitherto relatively untapped source of finance for the IFC — commercial insurers. In these transactions, IFC insures its B Loan participation in a commercial syndication. Upon transferring this risk, the value of the participation is no longer counted as an IFC commitment, thus increasing leverage. These types of transaction were cited as a possible reason why IFC's reported commitments from 2016 to 2018 were decreasing while IFC mobilisation was increasing. For a more thorough explanation of unfunded risk transfers, readers should access the 2019 MDB ***Mobilization*** report, where it is noted that unfunded risk transfers grew from 'negligible amounts in 2016 to over 10%' in 2019 (IFC, 2021).

A rightful scepticism of the mobilisation numbers could be mollified by greater transparency from the multilaterals, but there has been a decrease in the transparency of mobilisation reporting in the years since our previous work. By way of example, OECD was previously able to provide 'semi-aggregated' mobilisation data for the 2012–2015 period from the multilaterals but has been prevented from doing so for subsequent periods as these institutions invoked confidentiality concerns. Some multilaterals have also reduced their disclosure and reporting to the OECD in recent years. For example, in the most recent OECD report on mobilisation for 2017–2018, IFC reported one lump sum figure on mobilisation, IDB Invest did not report any data for 2018, citing confidentiality issues, and the African Development Bank did not report any mobilisation figures for 2018 (OECD, 2020b). Further, multilaterals invoking these confidentiality concerns seems to be at odds with the bilateral DFIs who were able to report more disaggregated mobilisation data to the OECD.

This lack of transparency undermines understanding and evidence-based policy discussion and decision-making and threatens the credibility of DFI and MDB reporting. For those that believe in the promise of DFIs and MDBs, it is a disappointing turn. That said, it should be acknowledged that the multilaterals and OECD have been working to resolve this issue and progress seems to be on the horizon. We understand that a data-sharing application has been agreed and developed that will allow the OECD access to multilateral data on mobilisation; this will strengthen the utility of OECD analysis. We hope and urge that this access is granted to other external stakeholders to support the provision of independent analysis and scrutiny to inform policy discussion and decision-making.

7 Reflections and the future of development finance institutions and multilateral development bank investing

The analysis in this report has provided an in-depth look at trends in DFI and MDB investment flows and the amounts that these investments have mobilised. It has highlighted positive trends of higher rates of reported mobilisation, increased investment in LMICs and increased investment in riskier countries; but it has also underlined that total DFI and MDB annual investment is growing quite slowly, that LICs continue to receive a paltry share of investment, and that DFIs and MDBs remain tied to employing instruments with which they have experience and capacity. These trends should anchor shareholder discussions on the role of DFIs and MDBs in supporting the 'build back better' agenda. Whilst progress has been made, it has been slow; without a bold change in approach this agenda will continue to veer off course. It is against this backdrop, supported by this analysis, that four crucial issues facing DFIs, MDBs and their shareholders are considered: the Covid-19 crisis response; the relationship between ODA and DFI/MDB investment; DFI and MDB investment in LICs; and the need for greater transparency from DFIs and MDBs. Although discussed separately, these are interlinked and will determine how DFIs and MDBs are viewed.

7.1 DFIs, MDBs and the Covid-19 crisis response

The most immediate issue facing developing countries is the impact of the Covid-19 crisis. These countries have significant amounts of public and private debt, a situation that has deteriorated since the beginning of 2020, and there are signs the sovereigns in the largest developing countries are facing less demand for their government debt (Wheatley, 2020). On the face of it, a government facing tighter debt markets may not immediately impact DFI and MDB investees that operate in these countries, but the linkages are real. A developing country that faces difficulty borrowing in an economic crisis is a country that is constrained in the ways it can stimulate its domestic economy. One way developed countries have responded to the Covid-19 crisis is through increased borrowing, passing this borrowing on to citizens via direct cash transfers. Theoretically, these citizens receive these transfers and spend it, keeping domestic businesses alive. In developing countries, some of these domestic businesses are DFI and MDB investees. While the G20 Debt Service Suspension Initiative has offered a temporary debt repayment moratorium to developing countries as a way of providing liquidity to these governments, developing countries are at the mercy of the debt buyers who understand the temporary nature of these measures, the debt scenario prior to the crisis and debt markets that are flooded with government offerings. This shows that support for investees must come from the DFIs and MDBs themselves and must take a long view as an economic recovery for many developing countries is not a part of their immediate futures.

DFIs and MDBs have responded quickly and flexibly to the crisis. While IFC, CDC Group and US DFC have rolled out new health-related initiatives that aim to strengthen healthcare systems in developing countries, the majority of the DFI and

MDB response has been to defer loan payments, provide working capital and liquidity, and extend trade finance to help protect existing jobs and livelihoods. In a sense, DFIs and MDBs have acted as a backstop to existing investees unable to rely on their own governments to do so. What has been less clear from DFIs and MDBs is (1) whether investees that have already taken on debt should take on more with uncertain demand for their product and services; (2) how long the DFIs and MDBs are willing to extend these programmes; and (3) how Covid-19 has affected DFI and MDB balance sheets and finances – for example, the impact of unrealised losses on equity portfolios, debt service rescheduling or write-offs, calls on guarantees etc.

These issues are raised because, as the data shows, DFIs and MDBs favour loans. They are simple, allow institutions to recycle capital, and provide DFIs and MDBs more certainty regarding returns on their investment. Loans are a staple for most DFIs and MDBs. Are these institutions, the businesses of which rely on one model, able to adapt that model to better meet the needs of their investees in the event of a crisis? DFIs and MDBs that have more equity investments in their portfolio are likely able to take a more patient approach and push the estimated timing of the return of their investment to a later period; but loan-driven DFIs and MDBs may not have that luxury. Moreover, some of these institutions are funded by capital markets and need to service their debt, which limits their ability to provide relief to clients. Even if temporarily feasible for the DFI or MDB lender, is providing more debt to already indebted firms the best way forward? Obviously, DFIs and MDBs would have done a certain level of due diligence when the original investment was made, but conditions have changed and the repayment of these original investments is less certain.

Alongside these questions about making tough decisions regarding further support to their investees, are questions about the ability of DFIs and MDBs to materially step up new investment in 2021 and the medium term. If DFIs and MDBs are creating new facilities, supporting prior investments with more funds and having less capital returned to them, their limited resources for new investments will decrease. Pre-crisis, many DFIs and MDBs had low returns on assets (ROAs). For example, IFC reports ROAs of 0.1% in 2019, 1.4% in 2018 and 1.6% in 2017. The average for the EDFI group was –1.32% in 2019, 0.6% in 2018 and 2.2% in 2017. These low ROAs suggest there is not a lot of room for manoeuvre. The pressure on their funding models is of concern considering our analysis, which has shown that investment is increasing at a slow rate, and that it is stubbornly low in LICs despite the increased need for investment to counter the decline in FDI. Going to their shareholders for increased funding may be a viable strategy for some DFIs and MDBs, but likely not for all. However, without increased funding, the runway for supporting investees and scaling investment is short. How DFIs and MDBs manage their own liquidity, which sectors and regions receive support, and using which instruments promises to be as informative to the long-term direction of DFIs and MDBs as it is to their short-term orientation.

7.2 Bilateral DFI investment and ODA

In December 2018, members of the OECD DAC agreed to a new set of interim rules whereby donor spending through private sector instruments would be reflected in the ODA figures each donor reports. These private sector instruments can be reported on an institutional basis or an instrument basis. With regard to the institutional basis, donors can now claim capital contributions to their DFIs as ODA, and reflows to the government from the DFI would count as negative ODA. This offers an opportunity for

bilateral DFIs to expand their balance sheets, expand on the type of work they have already been doing and respond to the Covid-19 crisis facing their clients. However, this accounting change has come with increased scrutiny as the new rules may incentivise donors to redirect ODA from traditional aid projects to DFIs if donors believe that they can mobilise private finance with this capital (Meeks et al., 2020).

As this accounting method is quite new, there has been little evidence so far of this redirecting and establishing a trend in the future, highlighting that donors are reallocating ODA will be difficult, especially as ODA budgets are cut.[36] Whether evidence of a reallocation can be established is not as important as the perception that is being formed – that donor allocations is a zero-sum game and that aid agencies and bilateral DFIs are now competing for funding. DFIs need to address this perception head on. They need to highlight their own comparative advantages over traditional channels of ODA and must be transparent on how they invest and on the development outcomes they deliver. They also need to shed light on areas in their investment that are complementary to traditional ODA. This type of proactive transparency will be all the more important as stakeholders assess how donor governments are allocating precious resources domestically and internationally in response to the Covid-19 crisis. DFIs are at risk of being seen as propping up foreign investors and foreign companies at the expense of helping the neediest around the globe. DFIs need to be mindful of these reactions and to explain the positive development outcomes that their investments have had and will continue to have if supported.

7.3 DFI and MDB investment in LICs

The poorest countries have fallen behind and the impact of Covid-19 on their economies and societies exacerbates the risk that they fall even further behind. As this report highlights, DFI and MDB investment remains stubbornly low in LICs; at the same time, FDI has fallen precipitously in LICs and private investment in infrastructure is negligible (Tyson, 2018). Shareholders of DFIs and MDBs, the institutions themselves, as well as donors must reflect on how DFI and MDB investment can more effectively support transformative growth in these countries. Mobilisation at scale in these markets will be difficult; emphasis should be on market creation. As it is possible that more ODA will be channelled through MDBs and DFIs, shareholders and these institutions must revisit and rethink their approach to their agenda in LICs (Meeks et al., 2020). Essentially, DFIs and MDBs will need to shift from a 'market taker' role responding to individual investment opportunities as and when they arise, to a 'market maker' role where DFIs and MDBs invest strategically to build and shape markets. This thinking and approach must address two fundamental issues that frustrate private investment in LICs. If addressed, they will have fundamental implications for the operations and financing of these institutions, and they will need to be understood and explored with shareholders. First, the level of country risk, and second, the lack of investible or near-market investible opportunities.

The first is a huge barrier and one that private sector operations of MDBs and DFIs cannot fix or,

36 For example, in July 2020, the UK Foreign Secretary announced a cut of £2.9 billion to the UK ODA budget in 2020. From 2021, the UK government announced that it will temporarily reduce its ODA to GNI target from 0.7% to 0.5%. It is estimated that the UK ODA budget will be cut by £4.7 billion from £15.2 billion in 2019 to £10.5 billion in 2021 (UK Parliament, 2020).

at least, cannot fix alone. There is an urgent need to refocus collective efforts on strengthening the investment climate in LICs. Here there is a clear role for government and a clear role for the public sector windows of the MDBs, regional development banks and donors to collaborate and support this upstream work. DFI and MDB investment should then follow and complement the reform agenda. Indeed, policy reform efforts may be made easier when accompanied by an MDB and DFI financing plan. MDBs and DFIs can play a critical role complementing reform but this requires a shift to a much more strategic and coordinated country approach. At the high end of ambition, this enhanced role could be organised around country compacts to involve key stakeholders, as advocated by Nancy Lee of the Center for Global Development. At a lower level of ambition, MDBs and DFIs could develop country private investment strategies that lay out how they plan to achieve market creation, and in which sectors, in these countries. These plans should clearly articulate how they wish to collaborate with other institutions: for example, how bilateral DFIs will partner with other development agencies upstream to build markets in their focus countries. This reorientation necessitates a different way of organising how investment is originated, with implications for MDB and DFI financing models.

MDBs and DFIs can play a critical role in addressing the second issue by focusing on pioneering, demonstration and early-stage investments for which there is a scarcity of investors. This requires increased levels of high-risk capital – in the form of grants, equity, mezzanine financing including convertible finance and contingent grants and guarantees, for example. Some MDBs and DFIs make use of these instruments but their use is not extensive, especially in LICs. Shifts in the instrument composition of MDB and DFI portfolios will again have implications for their capacity and financing models. MDBs and DFIs should also actively seek out, partner and build the capacity of suitable partners in LICs that can help build the pipeline, bring deals to the market, as well as tap and develop local capital markets. NDBs, as an example, could play an important role here — well-run NDBs have unrivalled knowledge of local markets and long-standing relationships with local private and public sectors. These competencies make certain NDBs great partners as they are uniquely placed to channel and mobilise public and private finance, both domestic and international (Griffith-Jones et al., 2020).

7.4 DFI and MDB investment transparency

The call for better data and better transparency is a common one for those analysing DFIs and MDBs (Kalow et al., 2016; Attridge and Engen, 2019; Kenny, 2020b). Whether it is better disclosure of investments (including improved DFI and MDB reporting in the OECD creditor reporting system[37]), documentation that supports investment additionality, or how impact is calculated, there are a host of issues on which DFIs and MDBs have been challenged regarding their data disclosures. In many respects, these challenges, and the responsiveness of the institutions, has meant that investment data has moderately improved in recent years. While still far from perfect, progress should be acknowledged.

Still, progress has been uneven, and reversals in some areas even more troubling, especially considering that core contributions to multilateral

37 As part of the OECD DAC provisional reporting arrangements on private sector instruments.

institutions are reportable as ODA and that bilateral DFI investment can now be counted as ODA under new OECD DAC rules. Despite great effort to engage with the multilateral institutions, this analysis had to use two different sets of data on amounts mobilised because multilateral parties to the OECD data collection requested privacy. As we have argued, it is not obvious what confidentiality considerations are broken if semi-aggregated mobilisation amounts by country income group, instrument and sector are disclosed by institution, with the possibility to redact in the event that one investment could be reverse engineered to reveal sensitive information. Similarly, although reporting of mobilisation data by the bilateral DFIs to the OECD has been improving, we have discovered instances of incomplete reporting. This lack of transparency breeds a credibility gap whereby DFIs and MDBs publish mobilisation figures and those outside these institutions have no way to make sense of the data. Worse yet, the two reports that are relied upon for this mobilisation data lack agreement on what should count as amounts mobilised.

The reason this inconsistency is particularly problematic is that it undermines the ability of stakeholders outside the organisations to objectively analyse and discuss how DFIs and MDBs are performing, as well as undermining trust in these institutions and the mobilisation agenda more broadly. The mobilisation of private finance is not the sole goal of DFIs and MDBs; of course, development impacts, financial return and financial/developmental additionality should also be part of the assessment of each DFI and MDB. However, mobilisation is very much the value-added of these institutions. Government owners can attain development impacts and financial returns from different ministries or agencies; what sets DFIs and MDBs apart from these other governmental institutions is their ability to work with the private sector. If these results are not offered in a manner that can be consistently studied and tracked, how can observers remain confident that DFIs and MDBs are the institutions best placed to meet these ends? As publicly funded and/or publicly guaranteed institutions, claims that releasing such data would violate the confidentiality conditions of investments makes one wonder why such confidentiality conditions were agreed to at the investment stage. Is the disclosure of how much private investment is included in a deal really a dealbreaker for private investors who, in many cases, are gaining access to concessional capital? For supporters of DFIs and MDBs, this step back in transparency undermines recent gains and hinders arguments that these organisations should be receiving more public funds.

7.5 Final reflections

2020 and 2021 have shown themselves to be the hardest period that DFIs and MDBs have faced since the global financial crisis of 2008. The Covid-19 crisis has adversely impacted clients, forced the DFIs and MDBs to work remotely, halted investment plans and undermined various other projects that these institutions had planned to undertake. The recovery trajectory is not yet known, but what is clear is that it will be different across regions and sectors. DFIs, MDBs and their stakeholders will be facing tough decisions, decisions that are likely to change the allocation of their portfolios and their future aspirations. This analysis has been intended to shed light on where DFIs and MDBs have been and where they could be going given these tumultuous times. With this evidence in hand, all stakeholders will be better informed when they make weighty decisions and navigate uncertain times.

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Appendix 1 Methodology

Definition of DFIs

Per the Association of European Development Finance Institutions (EDFI) (n.d.), DFIs are specialised development organisations that are usually majority owned by national governments. DFIs invest in private sector projects in LICs and MICs to promote job creation and sustainable economic growth.

DFIs can be bilateral, serving to implement their government's foreign development and cooperation policy, or multilateral, acting as private sector arms of international finance institutions (IFIs) established by more than one country.

For the purposes of this analysis, AFD and MIGA are also included despite not always being considered DFIs. The reason for the inclusion of AFD is that its and Proparco's operations were very intertwined over the study period and AFD had a significant portfolio of non-sovereign operations focused on development via private sector investment. Similarly, the majority of MIGA's guarantees are issued to private investors as a way to support private investment in developing countries.

Introduction to DFI investment

Data on DFI investment and the amounts of private finance mobilised by DFI investment is improving in some respects and has taken a step back in others. It was the intention of this analysis to expand on Attridge and Engen's (2019) previous work by including more DFIs and more recent data on the DFIs included in the previous report. With respect to the former, including FMO and DEG in this analysis, while expanding on the investment data of the AsDB, were positives that could be drawn from the data collection analysis. However, the depth of the analysis that could be performed was impeded by limits on the level of disaggregated mobilisation data that was provided by the OECD for the 2016–2018 period. Although some information was provided for the bilateral DFIs, no disaggregated data was provided for the multilateral institutions, due to confidentiality reasons, which forced the analysis to consider data provided by the *Mobilization of Private finance by multilateral development banks and development finance institutions* reports. As flagged in the analysis, the methodology used in OECD reporting and the other reports is not the same and undermines the exactitude of the analysis presented.

Determining mobilising commitments

The objective was to collect data on the amounts invested that were intended to mobilise private finance by the 12 selected institutions. Key to this data collection and subsequent coding was the assumption that not all DFI and MDB investment activities were aimed at mobilising private finance and that using

the total commitment data from the DFIs and MDBs would have overestimated the funds used for mobilisation. The analysis focused on the strategic use of development finance to mobilise additional private finance for development purposes.

To get a detailed picture of the institutions' commitments, as much disaggregated data as possible was collected. Specifically, the data had to be detailed enough to map which countries received the financing, in which sectors, using which instruments. When available, this information was drawn from public data sources; when not available, the DFIs provided the data directly.[38] From there, each investment was screened to determine whether or not it aimed to directly mobilise private finance. The following assumptions were made when assessing whether individual projects were identified as mobilising.

General

- Only non-sovereign operations were determined to be mobilising. All sovereign operations were excluded as it was assumed that these did not involve private financiers.
- For investments made by EIB, only investments in non-European Union and non-European Free Trade Association countries were considered as the focus of the analysis was on developing countries.[39]

Instruments

- All projects involving direct equity in private companies were treated as mobilising as it was assumed that the motivation behind direct investment was to attract further capital from private investors.
- All projects involving guarantees and insurance (to the private sector) were treated as mobilising as it was assumed that the intention of the guarantee/insurance was to unlock a private investment that would otherwise not have been undertaken.
- Projects involving investments in funds were treated as mobilising if the fund also involved other private investors. If the fund was only financed by DFIs or other public sources, it was not classified as mobilising. In cases where no information on the fund's investors was found, it was assumed it included private investors (as there tends to be more information on DFI-only funds).
- Projects involving lines of credit were treated as mobilising if the financial intermediary had to cover some of the cost of the sub-loans, take on some of the risk or provide some additional financing on top of the credit line. In practice, the EIB was the only institution to use this instrument and it does not disclose in its project descriptions the extent of the sub-loans it covered. Thus, all these investments were treated as mobilising as long as they went to a private sector intermediary.
- For projects involving loans, identification was more complicated. First, if the project description explicitly stated the loan was in the form of subordinated debt, B-loan or similar, it was classified as mobilising. Where this information was not available, the DFI commitment was compared with the

38 As noted in the analysis, AFD and Proparco only provided commitment data for 2016, 2017 and 2018. As a result, data for 2013 to 2015 was imputed based on the country, instrument, and sector shares derived from the 2016–2018 data and totals were derived based upon growth of AFD and Proparco commitments from 2013 to 2018 based on publicly available reports.

39 Bulgaria and Romania are the only European Union members considered to be middle income by the World Bank.

total project cost. If the total project cost was higher than the commitment, unless there was specific information suggesting the co-financer was a public investor, it was classified as mobilising. Note that this applied even if the co-financer was the investee/lending company. Loans made by CDC Group, DEG, FMO and Norfund, for which no information was available for total project cost, were assumed to be mobilising.

Further notes

Given the public information provided by AsDB, all investments were made using unknown instruments and were classified as mobilising. Information provided by DEG and FMO did not disclose total project amounts, so all investments were classified as mobilising.

Standardising datasets

Because of varying reporting standards, the institutions' datasets are not always directly comparable. To make them comparable, it was necessary to standardise the instruments, sectors and values of commitments to US dollars. Values were calculated to US dollars from their original currency based on the average exchange rate in the year of commitment as provided by the OECD (2020c).

Instruments

- Any investment in a fund was classified as 'funds', regardless of whether the instrument used was debt, equity or otherwise.
- Projects classified as risk management (at IFC) and risk participation (at CDC) were grouped into the 'risk management' instrument.
- For projects in which multiple instruments were used, the instrument classification used by the institution in its database was applied.

Sectors

As the sector classifications varied among the DFIs, translations were needed to standardise the sectors. These translations are shown in Table A1.

Income classifications

World Bank income classifications (LICs, LMICs, UMICs, high-income countries) were used to classify countries that received DFI investment and received mobilised private finance. For commitment analysis in Chapter 4 we used individual classifications for each project, based on the classification of the country on the date of commitment. For mobilisation data in Chapter 5, we use the country classification for the calendar year where disaggregated data is available; for MDBs we use their aggregated country income data reported for 2016–2018. Given that some countries were reclassified during the period under analysis, two projects in the same country (but at different times) can have different income classifications.

Income decile analysis

To provide more nuance regarding which countries are receiving more or less DFI investment and welcoming more or less mobilised private finance, the analysis looked at the income level deciles of the beneficiary countries. Each country that was classified as developing (non-high income) by way of the World Bank classification was classified into income-level deciles based on their respective GNI per capita for the given year. Countries that did not have GNI per capita data for a year were not included. As well, regional investments were not included as they were not made in a specific beneficiary country.

Sovereign risk rating analysis

Similar to the income decile analysis, beneficiary countries of DFI investment and mobilised private finance were classified based on the sovereign risk rating assigned to them by S&P Global Ratings. As risk ratings change at irregular intervals, a country was assumed to have had the same risk rating since the last time the rating changed or was confirmed. Regional investments were included by assigning a rating to the regions based on the median of those countries with a rating within that specific region.

'Amounts mobilised' data

As mentioned previously, the 'amounts mobilised' data was sourced from both the OECD and, in the case of the 2016–2018 period, data on the multilateral institutions was sourced from their own publications. The data collected and analysed from the *Mobilization of private finance by multilateral development banks and development finance institutions* reports was data related to private direct mobilisation and did not include indirect mobilisation figures. These private direct mobilisation figures were more aligned with the OECD's figures than disclosures that included indirect mobilisation figures.

Moreover, in *Mobilization of private finance by multilateral development banks and development finance institutions*, the EIB reports that a significant amount of its mobilisation is in the Europe region. This amount is unsurprising given that EIB predominantly invests in EU (European Union) and EFTA (European Free Trade Association) countries – countries which tend to also be high income. These Europe mobilisation amounts were excluded from any of the mobilisation analyses.

Finally, the 2012–2015 data provided by the OECD listed the country that mobilised the private finance, not the individual agency within the country. For the 2016–2018 period, the data provided by the OECD offered this nuance. To adjust for this difference, the share of a country's mobilised private finance that a DFI accounted for from 2016–2018 data was applied to the 2012–2015 data. For example, CDC Group accounted for 70.6% of private finance mobilised by the United Kingdom for 2016–2018, so the 2012–2015 amounts were adjusted so that CDC Group accounted for 70.6% of these amounts.

Table A1 Consolidated sector classifications

New classification	Banking and finance	Extractive sectors	Infrastructure	Other/multi-sector	Productive sectors	Social sectors
IFC	Financial institutions	Oil, gas and mining	Infrastructure; telecommunications, media and technology	Funds, other	Agribusiness and forestry; manufacturing; tourism, retail and property	Health and education
MIGA	Banking; capital markets; financial markets; financial services; leasing	Mining, oil and gas	Infrastructure; power; solid waste management; telecommunications; transportation; water; water and wastewater	–	Agribusiness; chemicals; manufacturing; manufacturing and services; services; tourism	–
IDA	Banking institutions; other non-bank financial institutions	Oil and gas; other energy and extractives	Energy transmission and distribution; non-renewable energy generation; other information and communications technologies; other transportation; power; railways; renewable energy: hydro/solar/wind; rural and inter-urban roads	–	Fisheries; forestry; other agriculture	Central government; health; other public administration; public administration – transportation
EIB	Credit lines	–	Composite infrastructure; energy; solid waste; telecommunications; transport; urban development; water, sewerage; telecom	–	Agriculture, fisheries and forestry; industry; services	Education; health

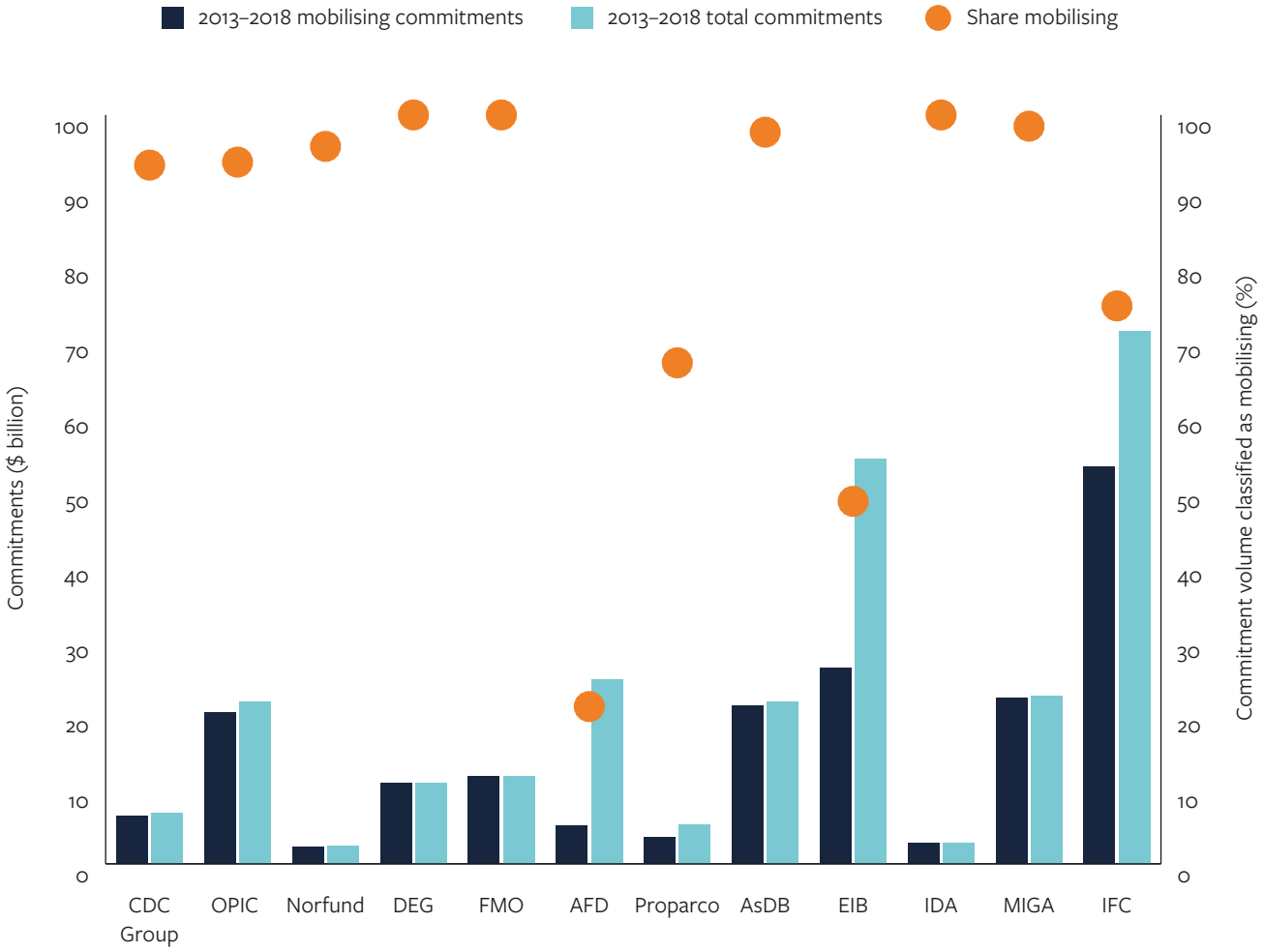
New classification	Banking and finance	Extractive sectors	Infrastructure	Other/multi-sector	Productive sectors	Social sectors
CDC	Financials – commercial banks; financials – consumer finance; financials – diversified financial services; financials – microfinance – institutions; financial services; financials – microfinance – SME banks	–	ICT – telecoms; infrastructure; telecom; technology	Financials – funds; multisector; SMEs	Agribusiness and food; consumer – general; industrials; real estate; food and agriculture; forestry; manufacturing	Education – core education; healthcare – healthcare providers and services; healthcare – life sciences tools and services; health; education
OPIC	Financial services; finance and insurance	Extractives; mining, quarrying, oil and gas extraction	ICT; infrastructure; information; utilities; construction; transportation and warehousing	General; humanitarian assistance	Agriculture; agriculture, forestry, fishing and hunting; hospitality and tourism; industrial; manufacturing; real estate, rental and leasing; retail trade; accommodation and food services; tourism, real estate and retail trade; professional, scientific and technical services; other services (except public administration); administrative and support, waste management and remediation services; arts, entertainment and recreation; wholesale trade; services	Educational services; healthcare; healthcare and social assistance; healthcare and educational services
AFD/Proparco	24030–25020	32210–32268	21010–23640	Everything else	31110–32182, 32310–33210	11110–16064

New classification	Banking and finance	Extractive sectors	Infrastructure	Other/multi-sector	Productive sectors	Social sectors
Norfund	Banking; financial services; microfinance; financial institutions	–	Energy; clean energy; renewable energy	Investment funds; Balkan Trustfund; SME Funds	Agriculture; food and agribusiness; manufacturing; other industrial partnerships; other services; tourism; industrial partnerships; food and agri	–
FMO	Financial institutions	–	Energy	Diverse sectors; multisector fund investment	Agri, food and water	–

New classification	Banking and finance	Extractive sectors	Infrastructure	Other/multi-sector	Productive sectors	Social sectors
DEG	Activities auxiliary to financial services and insurance activities; financial service activities, except insurance and pension funding; insurance, reinsurance and pension funding, except compulsory social security	Mining of coal and lignite; other mining and quarrying	Air transport; construction of buildings; electricity, gas, steam and air conditioning supply; energy; land transport and transport via pipelines; sewerage; telecommunications; water collection, treatment and supply	–	Accommodation; activities of head offices; management consultancy activities; architectural and engineering activities; technical testing and analysis; computer programming, consultancy and related activities; creative, arts and entertainment activities; crop and animal production, hunting and related service activities; food and beverage service activities; forestry and logging; information service activities; manufacture of: basic metals; basic pharmaceutical products and pharmaceutical preparations; beverages; chemicals and chemical products; computer, electronic and optical products; electrical equipment; fabricated metal products, except machinery and equipment; food products; furniture; leather and related products; machinery and equipment, not elsewhere classified; motor vehicles, trailers and semi-trailers; other non-metallic mineral products; paper and paper products; rubber and plastic products; textiles; wearing apparel; wood and products of wood and cork, except furniture; articles of straw and plaiting materials; manufacturing; other manufacturing; other professional, scientific and technical activities; printing and reproduction of recorded media; programming and broadcasting activities; retail trade, except of motor vehicles and motorcycles; security and investigation activities; warehousing and support activities for transportation; wholesale and retail trade and repair of motor vehicles and motorcycles; wholesale trade, except of motor vehicles and motorcycles	Education; human health activities

Appendix 2 Analysis of mobilising and total commitments

Figure A1 Comparison of total annual commitments and mobilising commitments

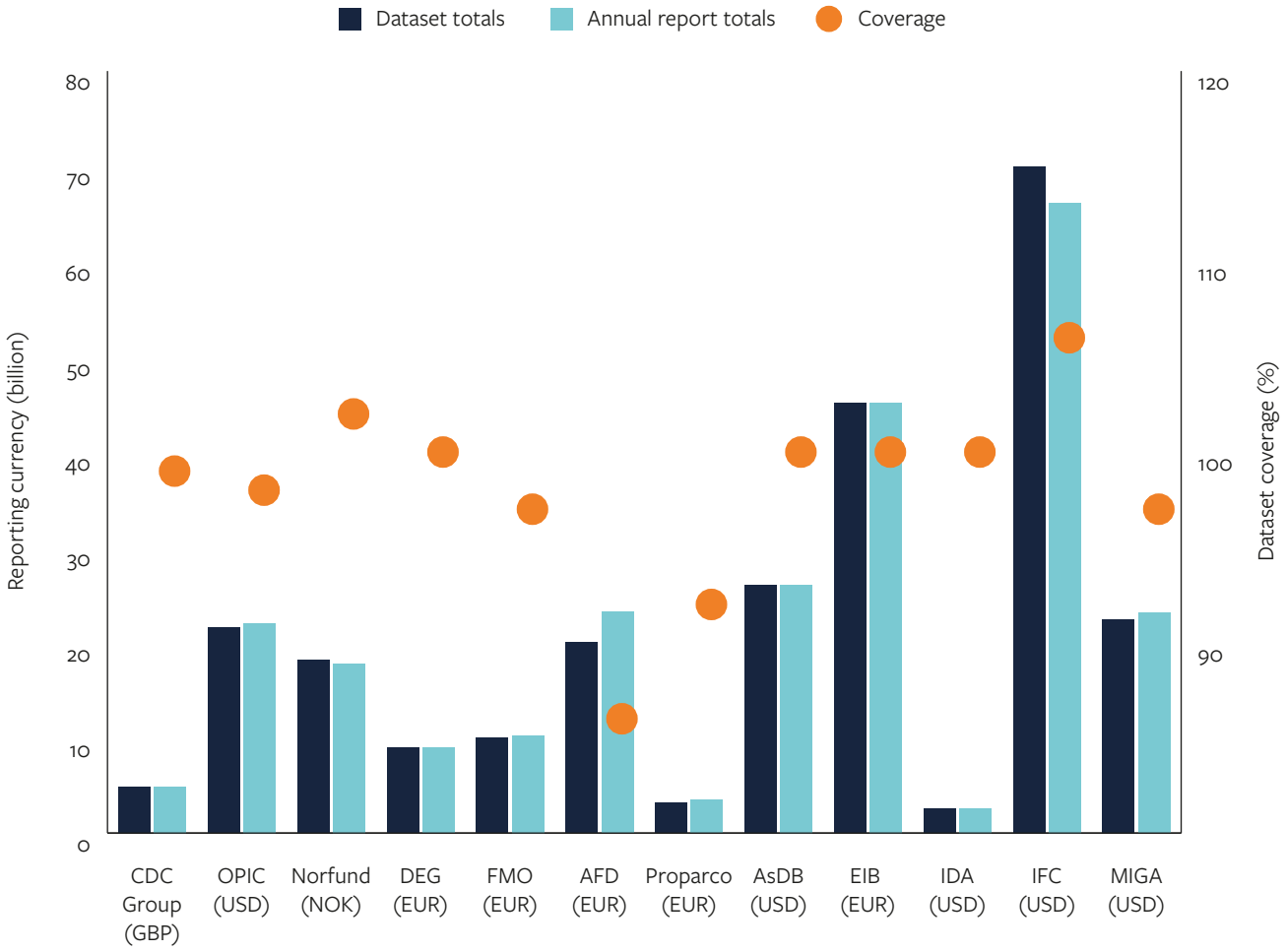


Note: AFD and Proparco data are imputed for 2013 to 2015.

Source: Authors' calculations based on ODI dataset

Appendix 3 Accuracy of datasets to annual reports

Figure A2 Comparison of total annual commitments, project-level datasets versus annual reports



Source: Authors' calculations based on ODI dataset and DFIs' annual reports